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No. 11

POLITICAL (EXTERNAL) DEPARTMENT. COLLECTION.

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China

GENERAL HEADING

1930 to

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Notes:

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CHINA April 1, 1947 Section 1

Copy No. 16

ANNUAL REPORT ON CHINA, 1946

Sir R. Stevenson to Mr. Bevin. (Received 1st April)

(No. 145)

Sir, Nanking, 14th March, 1947 I have the honour to enclose herein a brief but comprehensive survey of China for the year 1946, for which I am indebted to Mr. G. A. Wallinger, His Majesty's Minister at this embassy.

I have, &c.
RALPH SKRINE STEVENSON.

Enclosure

Annual Report on China, 1946

President Truman's statement of China policy on 15th December, 1945, the arrival in China of General Marshall a few days later, and the declaration of the three Foreign Ministers at Moscow on 17th December had combined to produce an artificial détente in the political atmosphere in China at the beginning of 1946. Moreover, these influences from outside had followed upon a visit of Chairman Mao Tze-tung from Yenan to Chungking and the reappointment of General Chou En-lai as Communist representative resident in the capital. The possibilities for a settlement of the Kuomintang-Communist dispute therefore seemed brighter in January 1946 than ever before; and in fact agreement was reached early in the month for the cessation of hostilities and the restora-tion of communications. The first result of this accord was that a Political Consultative Conference of all parties met on 10th January in an atmosphere of some optimism. The deep-seated and mutual distrust between the Communists and the Knomintang admittedly continued, and the reactionary groups of the latter were certainly no less active in sabotaging any attempts at compromise; but it did seem that, at long last, the force of economic facts and the interests of the people of China might be allowed some weight in the political balance. On the Communist side at least (whatever the ultimate objectives of the party) it seemed that horse-trading rather than intransigence was the order

of the day; their attitude was doubtless affected by the realisation that, as the tasks of reoccupation in the south were finished, the Kuomintang would have a relatively high military potential with several American-trained and equipped divisions to throw in in the north. On the Kuomintang side the wiser heads seemed to appreciate that the American economic aid essential to China's reconstruction would not be so readily forthcoming if the party failed to make a genuine bid for political compromise.

2. The Political Consultative Conference meetings continued, with heated interchanges, until 31st January, when a series of agreements were announced covering the reorganisation of the Government, national reconstruction, army reorganisation, the National Assembly and the draft Constitution. Salient provisions of these agreements stipulated: the creation of a State Council to supersede the Supreme National Defence Council as China's highest administrative authority; the admission of minority party representatives into the Executive Yuan; the convening of the National Assembly with its 1936 membership, but with additional delegates representing new political and professional groups; the revision of the existing draft Constitution by a special committee representing all components of the Political Conference; and the Consultative reorganisation of the Legislative Yuan as an elected body bearing some resemblance to a parliamentary chamber. The settlement of the vital question of the control over the independent armies of the Chinese Communist Party was, however, left to a three-man committee under General Marshall, and realists noted that the constitutional problem, to which the Communists also attached great importance, had really only been transferred to another

3. The agreements did, however, seem to constitute a victory for the more reasonable elements on both sides, and there appeared at least some possibility that,

deliberating body.

with General Marshall's advice and American "umpires" to see fair play, a modus vivendi could be reached. The socalled "Executive Headquarters" were quickly set up in Peking as the operations section of General Marshall's three-man committee, with American, Kuomintang and Communist representations and a brief to tackle all problems arising out of the armistice; and "field teams," also tripartite, were beginning to proceed under the orders of the headquarters to areas where friction and incidents had occurred. What was needed for success was good faith on both sides; but, in fact, it was only a matter of days after the declaration of the armistice that the respective propagandists, who were dangerously irresponsible throughout the year, started flinging accusations at each other of contraventions

4. Even more serious as a disruptive factor was the situation in Manchuria, where what His Majesty's Embassy at Moscow have described at the "elemental kleptomania" of the Soviet troops had aroused fear and resentment, which led in mid-February to student demonstrations, probably Government inspired, in Chungking and other centres. Meanwhile, with the aid of American aircraft, a steady trickle of Central Government troops and officials were being flown into Manchuria as far north as Mukden; and, at the end of the month, strengthened perhaps by the above-mentioned demonstrations. Minister for Foreign Affairs announced that he had asked the Soviet Ambassador about the intentions of his Government both as to the withdrawal of Soviet troops and the disposal of stocks and machinery in the province. At the same time it was becoming clear that, despite the armistice agreement. Communist troops had pushed forward into Jehol and were beginning to infiltrate into those parts of Manchuria which the Central Government forces had not been able to occupy. From Chungking, it was difficult to judge whether the Communist or the Government forces were the first to infringe the armistice, and it is probable that each party exploited the possibility of pushing forward where the other party was weak; but the Sino-Soviet Treaty and the Japanese armistice terms both gave the Central Government the right to move into Manchuria, and there can be no doubt that the Communist advance in that area and their consolidation of a strong base at Kalgan in Jehol constituted a threat which subsequent events proved to have been serious. On the other side, however, the meeting of the

Kuomintang's Central Executive Committee early in March showed clearly that the controlling element in the party were by no means disposed to abide by the Political Consultative Conference agreements.

5. In these circumstances the agree ont which was reached by the three-man committee under General Marshall late in February, regarding the reorganisation of the army into integrated commands with established proportions of Government and Communist divisions in the various areas, was a less hopeful achievement than had at first seemed probable; and meanwhile the committee to discuss the Constitution was floundering in a morass of sterile argument. The above-mentioned demonstration of strength in the Central Executive Committee by the Kuomintang's "C.C. clique" inevitably resulted in exacerbating Government-Communist relations, and by the end of March it began to appear that, thwarted by General Marshall in the military arena, the reactionaries might succeed in destroying the whole rickety construction of agreement by their bitter opposition to any progressive thinking on constitutional issues. The situation was, moreover, not helped by the fact that, in those areas which had been taken over by Government administrators, their venality inefficiency had already more than neutralised the goodwill extended to them by populations which now found themselves exploited by monopolistic Government organisations and underpaid officials, and the prey of black-marketeers of all kinds.

6. At the end of March the Minister for Foreign Affairs announced a Soviet undertaking that their troops would be withdrawn from Manchuria by the end of April. This undertaking, desirable as it appeared, was actually an embarrassment to the Central Government, for a concentration of Chinese Communist troops at Ssupingkai, on the railway between Mukden and Changehun, and the effective military occupation of Shantung and Northern Kiangsu by considerable Communist forces posed problems which greatly complicated the task of the Central Government in taking over from the Russians. existence of these Communist occupying forces in Manchuria was underlined when "field teams" from the Peking Executive headquarters started to operate in the province. This was a notable extension of their terms of reference and de facto recognition was thereby given by the Americans to a situation which the existing agreements, both between the Government and the Communists and between the Government and the Soviet Union, should have excluded. The fact was that the Soviet commanders were handing over control of evacuation areas to the first arrivals, and in most cases these were Communist units. It is generally accepted at this was done by arrangement.

7. In Chungking the Generalissimo himself, who had not hitherto openly taken the part of his reactionary colleagues, found it necessary, early in April, to be outspokenly critical of Communist "illegal" activities in the north-east. As time went on it became known that Communist forces. certainly with Soviet connivance, had occupied Harbin and Changchun, that they had formed guerrilla units as far east as Antung and Kirin, and that they had acquired important stocks of equipment from the reserves of the Japanese Kuantung armies. Meanwhile the constitutional negotiations had broken down and the meeting of the National Assembly, long advertised for 5th May, was indefinitely postponed as a result of the refusal of the Communists and the Democratic League to appoint delegates to attend it.

8. It was in this atmosphere of opportunistic manœuvrings and embittered distrust that the capital was transferred from Chungking to Nanking. It was a bare pretence to claim that there was now no civil war, and it appeared that the only reason why there had not been an open break was because General Marshall was still in China. In May, despite the peripatetic activities of negotiators and mediators, the centre of interest in the conflict shifted quite definitely from the conference table to the field of battle, and it appeared that the Generalissimo had agreed to do what his military leaders had long advised and to seek a settlement by force of arms.

9. His campaign in Manchuria started well with a considerable victory at Ssupingkai and the consequent capture of Changchun; and he followed up his advantage by issuing a fifteen-day cease-fire order on 7th June, during which, he stipulated, terms for stopping hostilities in Manchuria and for the restoration of communications in China as a whole must be agreed. A prolongation of the truce for one week failed to produce agreement, and the published demands of the Communists were, in fact, such that the Generalissimo could not seriously have been expected to consider them. While both sides were undoubtedly prevaricating, it began to be clear to unbiased observers that the Communist attitude was now stiffening to such an extent as to cast doubts upon their desire

for any compromise. Yenan's propaganda had begun at this stage to take a strongly anti-American line and General Chou En-lai in Nanking took refuge, in his public statements, in cloudy generalisations and procedural arguments. The effect was to strengthen the hands of the diehards in the Kuomintang, and the first result was an announcement early in July that the National Assembly would meet, with or without the Communists, on 12th November, a move which called forth a more than usually violent flood of criticism from Yenan. The Generalissimo retired to summer quarters at Kuling; and Dr. Leighton Stuart, the newly appointed American Ambassador, with a long and honourable career behind him as a missionary educator in China, proceeded there to present his credentials at a time when the negotiations were almost dead and fighting in Northern Kiangsu was marking the beginning of a series of campaigns which culminated in the capture by the Government forces of Changteh (Jehol), Kalgan and Antung. The assassination in July of two prominent leaders of the Democratic League in Kunming emphasised the intention of the extremists of the Kuomintang to crush opposition by force.

10. From the standpoint of the American mediators, these developments were embarrassing, and the Generalissimo's apparent determination to seek a solution by force of arms drove them in mid-August to issue a statement serving notice on both sides that American patience was wearing thin. At the same time military aid was stopped and the usufruct of the \$500 million Import-Export Bank Loan to China was withheld. The Chinese Government did, however, obtain on 31st August an agreement by which she took over American non-warlike surplus stores from the Pacific Islands in settlement of the outstanding American debt to China for services to the United States armed forces in China during the war.

11. The Marshall-Stuart pronouncement seemed to shake the confidence of the Generalissimo, and at the end of August, by which time Government forces had made considerable territorial gains, he again opened the door to negotiations by agreeing to the formation of a five-man committee under the American Ambassador with two Government and two Communist members, which would be a political body and would concern itself with the formation of the State Council approved by the Political Consultative Conference agreements. Once again the Communists hung back and appeared thereby, from the standpoint of

to be subjected to leverage. On such issues as the opening of the Yangtze ports to foreign vessels, the political pull and selfish opportunism of Chinese vested interests combined to defeat all British attempts to develop trade and to override the obvious economic advantage to China of such

development.

20. As regards the taking over of the various International Settlements and foreign concessions, strenuous negotiation during the year finally broke down the Chinese intention to proceed to a unilateral assessment of the rights and obligations which China has inherited and the principle of joint assessment by ad hoc bodies in the places concerned has been accepted. A start has thus been made to clear up this knotty and important problem, and some progress has also been made, particularly in Shanghai, over the equally complicated task of re-registering property, with the local Chinese land authorities.

21. As in other parts of the Far East, nationalism was rampant in China and, although general xenophobia was happily absent, incidents with American troops and the virulent anti-Americanism of Communist propaganda were clear danger

signals.

Economic and Financial

22. Shortly before Christmas of the year under review it began to appear as if the inflation which had been held in check for several years might be about to overrun the system of controls devised by Dr. Soong to keep it in check. The problems of reoccupation and rehabilitation would by them selves have placed a heavy burden on China's economy in 1946 even had she been able to solve her political crisis and therefore to devote her resources to the task; but this was not the case and, although a measure of American economic aid was forthcoming, by the end of the year it had become clear that the political implications of internal strife were adversely affecting China's hopes of that aid-which had really become her sole hope. No major rehabilitation of trade, industry or internal communications were possible, and as 1946 creaked to its end, it began to appear that the efforts of Dr. Soong to maintain a

measure of control of the inflation by the sale of China's considerable holdings of gold and foreign currency were failing. Confidence, never high, was dwindling rapidly as people began to see that the stock must be exhausted soon and that the stringent import controls which had introduced earlier in the year could not hope to stem the tide; and as confidence decreased, speculation increased.

23. The total amount of the Chinese budget for 1946 was CNC 2,400 milliard and was overspent in the first seven months of the year. It has been estimated that total expenditure for the year was CNC 7,500 milliard, and that more than 70 per cent. of this great sum was used for military expenditure. The budget for 1947 has been set at CNC 9,500 milliard, of which only 36 per cent. is allocated to military expenditure, an allocation which was by no means justified by the prospects at the end of the year of a settlement of the civil strife. A budget deficit of CNC 2,300 milliard already appears in the estimates for 1947, and this figure is certainly entirely fictitious.

24. At the beginning of 1946 the Central Bank's exchange rate was fixed at CNC 2,020 to 1 United States dollar, and sterling cheques were to be negotiated at that time at rates up to about CNC 7,500 to the £. The American dollar rate on the "open" market gradually slid away from this rate, and on 19th August the Chinese Government lowered the exchange value of the currency by 40 per cent., and the official rate applicable for the rest of the year was CNC 3,250 to 1 United States dollar. For some time the level was fairly successfully held, but the fall, when it came, was rapid and serious, so that on 23rd December the open market rate for the dollar reached CNC 7,800. Heavy gold sales by the Central Bank and profit taking by the speculators caused a reaction and the rate at the end of the year was about CNC 6,500 to the dollar; but nobody believed that this or any other rate could be held and it become clear that a major crise de confiance was likely to come at any time. In the event, it was not long delayed, but that story is outside the compass of the present survey. paners when it was the many are when it is a set of the many is a set of the many in the many is a set of the many in a set of the many is a set of the many in the many is a set of the many in the many is a set of the many in the many is a set of the many in the many in the many in the many in the many is a set of the many in th INDEXED

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CHINA.

1939 ANNUAL REPORT, 1938.

[F 3662/53/10]

Sir A. Clark Kerr to Viscount Halifax.—(Received April 15.)

(No. 212. Confidential.) My Lord,

Shanghai, February 28, 1939.

I HAVE the honour to transmit to your Lordship herewith the annual report on China for 1938.

2. I am indebted to Mr. W. D. Allen, third secretary at this embassy, for the main part of this report, to Lieutenant-Colonel C. R. Spear and Group Captain R. S. Aitken, respectively military and air attachés, for the sections describing the military and air operations, and to Mr. A. H. George, commercial counsellor, Mr. R. H. Scott, commercial secretary, and Mr. Vice-Consul C. T. Crowe for the greater part of the chapter on trade and investment.

I have, &c.

ARCHIBALD CLARK KERR.

Enclosure.

Annual Report on China for 1938.

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I.—Introduction.

MEASURED in terms of human anguish, there has probably never been, even in the long history of Chinese suffering, such a year as 1938. The Japanese invasion has meant the devastation of vast regions of the richest provinces of China, the destruction of scores of cities by fire, bomb and cannon, the killing of numberless peasants and townsfolk, the shifting of millions of people, with all the misery and horrors that go with forced migrations, floods, famine and pestilence. Added to this there has been an almost unbroken series of military defeats, in the course of which hundreds of thousands of young Chinese, half trained, poorly armed and badly led, have lost their lives. More than enough to daunt the courage of a people. But the people hold out and the Government, which has seen the successive loss of ports, railways, industries and revenue, holds out too.

- 2. To have met with such a buffeting and to have withstood it would have been remarkable in any people. In the Chinese it has been all the more so because it has been unexpected. It has taken us all by surprise. It has disconcerted the Japanese and thrown them out of gear. The Chinese themselves share some of this surprise and draw fresh strength from this very fact. And having found their feet, as it were, they are determined to stand. It may thus be said that the past year and a half of war has brought forth a new spirit in China, or, better still, has purified and transmuted the spirit of new China, which, for some ten years or so, had been taking shape slowly and uncertainly—a spirit whose promise had hardly more than pricked the imagination of the Chinese themselves. Left to them, gestation and travail would have been long and painful. But the Japanese jolted the thing into life. It has been a robust birth. Of its present lustiness, indeed, the Japanese seem to have but little conception.
- 3. But the Japanese have done more than this for China. By marking him down as their especial enemy and by refusing to treat with him, they have given to China the man she needed in her time of crisis, a leader whose name, from the Great Wall to the Gulf of Tongking, stands as the symbol of everything upon which the modern Chinese put a value—unity, independence, the promise of democracy and hope for the future, all of which, a short time ago, seemed to be beyond their reach. These things and this man they are decided not to let go.
- 4. It is this that has made possible the resistance which has baffled the Japanese. The Chinese themselves claim and believe that in the end it will prevail. Time, they say, is on their side. They have but to hold on, to bend when pressed, but not to break, and, meanwhile, to pursue the gadfly tactics which they are in the process of perfecting. Their morale, they maintain, will outstay that of the Japanese. When one is amongst them in Central China it is hard to withstand the contagion of their optimism.
- 5. In their turn, the Japanese see things in a different way. They tend to find in this resistance not something that has been so far mainly Chinese, but something that springs purely from help from outside and principally from ourselves. Here they are clearly wrong, for until now His Majesty's Government have been able to do but little to make Chinese resistance effective. Conversations with Japanese show that they themselves have not begun to understand that the old scheme of things in China, upon which their policy is based, has passed, and that a fresh set of problems lies before them. They do not admit the existence of the new spirit of which mention has been made. They have shown that the success of their policy depends upon a large measure of Chinese co-operation and that they count upon it. But this the Chinese are resolved to withhold.
- 6. When the Japanese armies were closing in on Hankow, Mr. Masayuki Tani, the Japanese Minister at large, used to say that, so soon as this phase of the hostilities, which was to put a crown upon the campaign, was brought to an end, the Central Government of China would dwindle into a purely local régime. General Chiang Kai-shek would become no more than a rebellious warlord, without prestige or influence. And then there would rise up scores of

reputable Chinese ready and eager to co-operate with the Japanese in the setting up of a new Central Government in Nanking. When doubt was cast upon these hopes Mr. Tani would reply that he was already in touch with these reputable Chinese, and that the distinction of their names would surprise the world and destroy once and for all the empty myth of Chiang Kai-shek. Mr. Tani was disquietingly sure of what he said. But four months have now passed since Hankow fell, and no reputable Chinese has come forward to betray his country and to serve the Japanese. The excursion of Mr. Wang Ching-wei to Hanoi is no justification of Mr. Tani's confidence. It has been so far wholly ineffective and has only served to purify and strengthen the Central Government. In the north the Japanese efforts have been equally unavailing, for Marshal Wu Pei-fu has continued to play a game of puss in the corner, which has meant for them the losing of much face. In fact, General Chiang Kai-shek's prestige and influence remain undiminished.

While, therefore, the Chinese show no sign of faltering in their will to resist the Japanese aggression, which they have so far sustained mainly by their own effort, their power of endurance will tend, as time goes by, more and more to depend upon the help which they get from abroad. The moral effect of the recent American loan, combined with the promise of credits from Great Britain, has been very great; while the American note to Japan, about the Nine-Power Treaty, the "open door" and equal opportunity, and the parallel note, early in 1939, from Great Britain, have had a heartening effect which it would be hard to over-estimate. For the moment the Chinese are content in the belief that things are moving in the right direction, but they would like to see a further step taken in the shape of economic pressure upon Japan, which, they are persuaded, would be effective, a view which is shared by His Majesty's Embassies both in Tokyo and China. They do not ask for armed intervention, for they appreciate that the present situation in Europe precludes us from giving it, and they set no hopes in the sailing of an American armada across the Pacific, but they continue to plead for economic retaliation on the part of the democracies, seeing in it the speedy collapse of Japan. They have not been encouraged to believe that such retaliation is likely to be put into effect, but they are convinced that sooner or later force of circumstances will bring it about and so put an end to their present agony.

II.—INTERNAL SITUATION.

(a) Sino-Japanese Hostilities.

Military Operations.

General.

- 8. At the end of 1937 the Japanese, as the result of about six months' fighting, were in possession of Hopei, Chahar and Suiyuan. They had consolidated their position in the Peiping-Tientsin area and overrun a considerable area of Shantung and Shansi.
- 9. In Central China they had passed over an important part of Kiangsu, occupying Shanghai (except for the foreign-controlled areas), and the capital, Nanking. Hangchow, the capital of Chekiang, was also in their possession.
- 10. Japan had hoped that with the fall of Nanking organised resistance on the part of the Chinese would come to an end, but, although badly disorganised as a result of the fighting at Shanghai and Nanking, General Chiang Kai-shek succeeded in extricating the majority of his troops, and set about their reorganisation forthwith. It became necessary, therefore, for the Japanese to carry out further large-scale operations against the Chinese armies.
- 11. There were at that time two Japanese armies operating in China, one in the north under the command of General Terauchi, and the other in the Yangtze Valley, under the command of General Matsui. In October 1938 a third army, under the command of General Furusho, invaded Kwangtung and occupied Canton after a very brief campaign.

[19326]

Operations in North China.

12. In North China military operations during 1938 consisted mainly of movements southwards along the Tientsin-Pukow and Peking-Hankow Railways.

13. During the advance down the former the most bitterly contested action took place at Hsuchowfu, during which the Chinese inflicted a serious local reverse on the Japanese troops in the fighting for Taierchwang. Here, on the 7th April, General Chiang Kai-shek's troops, assuming an offensive rôle, compelled the Japanese to withdraw from the town. The Chinese failed, however, to follow up their success and the initiative soon passed again to the Japanese. By the 19th May the important town of Hsuchowfu at the junction of the Tientsin–Pukow and Lunghai Railways was in Japanese hands.

14. Casualties in this operation are reported to have been :-

Chinese: 120,000 (including 51,000 dead). Japanese: 21,500 (including 4,260 dead).

Simultaneously with the advance down the railway lines, Japanese columns were operating in Shansi Province, and by the end of February the line of the Yellow River had been reached at Liulin, west of Taiyuanfu. Subsequently operations took place in the south-west of the province, and by the 8th March Tungkwan, an important station on the Lunghai Railway, had come under shell fire from the north bank of the Yellow River. In the north-west of the province the Yellow River was reached at Paoteh and Hoken, and by the end of March the Japanese were in control of all main crossings between Paotow (West Suiyuan) and Fengkiu (North-East Honan).

15. In Eastern Shantung, Tsingtao was occupied on the 10th January and Chefoo on the 3rd February. In the southern part of this province, Japanese units cut the Lunghai Railway at Tangshan, west of Hsuchowfu, on the 14th May. On the 2nd June a Japanese advance in the direction of Kaifeng was started, and this town was occupied on the 6th June.

16. During June 1938 the Chinese breached the dykes of the Yellow River, which caused the Japanese to alter their plans and to hold up their advance.

17. A lull in the operations in the northern theatre now ensued, and interest shifted for the next few months to the Yangtze Valley.

Operations in the Yangtze Valley.

18. During the early part of 1938 activities in this area were confined mainly to mopping-up operations.

19. About the middle of June Japanese naval units advanced up-river, with subsequent army landings at Anking and elsewhere. On the 3rd July a passage was forced through the boom across the Yangtze at Matang—a position which was considered by the German Military Advisers to be impregnable. The necessity for mopping-up operations and the excessive heat in the valley at this time of year militated against any major scale operations during the first half of July. On the 26th July Kiukiang was occupied by Japanese forces, and subsequently the advance was continued along both banks of the river. The advance of the Japanese army was materially assisted by the co-operation of the navy. By the early part of August the Japanese had increased their forces in the Yangtze Valley to five divisions—two on each bank and one in reserve near Anking.

20. The Japanese now continued their advance on both banks of the river, and on the 2nd August were in possession of Susung on the north bank. Along the south bank their advance was directed on Juichang, which they captured on the 25th August, and, assisted by naval co-operation, advanced subsequently westwards towards the Kiangsi-Hupeh border and north-westward to secure from the land side the narrows on the Yangtze opposite Wusueh. The situation on the north bank during this period remained unaltered.

21. During September the fighting on the south bank was in two directions—westwards from Juichang to protect the advance of the navy, and southwards towards Teian. Chinese resistance in the latter area was very stubborn, and the Japanese lost heavily in some of their advances.

- 22. Operations to clear the Yangtze were continuous and successful, despite determined Chinese resistance in strong defensive positions. At the same time the Japanese force moving westwards from Juichang was making good progress.
- 23. North of the Yangtze, columns from Honan advanced southward, occupying Kuangshan and Hoshan on the 20th and 21st September respectively. Sinyang, an important town on the Peking-Hankow Railway, was occupied on the 12th October. The continued Japanese advance up the Yangtze and inland from its south bank meant a definite weakening of the Hankow defences, which, in this area, depended on a mass of hilly country covering Hwangshihkang, Tayeh to the west, and the country south of Yangsin. The last-named place fell on the 18th October. The Japanese forces continued their pincer movements, and, with Chinese resistance weakening every day, the first troops of the advancing army entered Hankow on the afternoon of the 25th October.
- 24. The Chinese evacuated Hankow after setting fire to large portions of the city and practically destroying the Japanese Concession. Wuchang and Hanyang were occupied on the 26th October.
- 25. After the fall of Hankow, Japanese columns from Wuchang, with naval co-operation, pushed on up-river and captured Yochow on the 12th November. The immediate effect of this latest success was to spread panic in Changsha, the capital of Hunan, which was set on fire by the Chinese in the early hours of the 13th November and burnt for five days.
- 26. The remaining weeks of 1938 in this area were spent in mopping-up operations and consolidation.

Operations in South China.

27. Concurrently with the closing stages of the advance on Hankow the Japanese effected a successful landing at Bias Bay on the 12th October with the object of cutting the Canton–Kowloon Railway and capturing Canton. In spite of the fact that the country in this area is naturally favourable to defence, and that elaborate preparations lasting over a year had been made to guard against the eventuality of a Japanese landing here, virtually no opposition was offered by the Chinese. Casualties suffered by the invaders were practically negligible, and, advancing in four columns, the leading Japanese troops entered Canton on the 21st October, after an advance the rate of which would compare very favourably with any routine peace march. This sudden and quite unexpected surrender of such an important centre by the Chinese gave rise to considerable speculation, but the question whether the disaster was due to corruption or ineptitude remains in doubt.

Guerrilla Activities.

- 28. During 1938 considerable guerrilla activity has been in evidence. The main Chinese forces pursuing these tactics are the VIIIth Route Army under the command of General Chu Teh, and the IVth Newly Organised Army with General Yeh Ting as its commander. The former army operates in the Provinces of Shansi, Hopei and Chahar, while the IVth Newly Organised Army has as its sphere of operations the Provinces of Anhwei, Kiangsu, Chekiang and East Kwantung. These armies are composed of men of communistic ideas.
- 29. The main scene of their activities during the year has been the Province of Shansi, where considerable interference has been caused to the Japanese lines of communications—trains being derailed, bridges blown up, and attacks on isolated Japanese posts carried out.
- 30. Although there is no doubt that the operations of the VIIIth Route Army have prevented the Japanese from obtaining anything approaching satisfactory control over the Province of Shansi, it must be admitted that guerrilla warfare, which should be synonymous with organised resistance by the entire armed civil population, has neither yet reached such proportions nor achieved such results as should be possible with proper guidance. Up to the end of 1938, it is doubtful whether the guerrillas had any effect on the course of the main campaign.

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Casualties.

- 31. In a country such as China it is difficult to get any accurate data regarding the casualties suffered by the opposing sides. It is fairly certain that the Japanese suffered heavy casualties during the advance on Hankow in 1938. It is estimated that their total casualties, including killed, wounded, died of disease and sick, amounted to 250,000(') since the opening of the hostilities. Seventy-five thousand of these are believed to have been killed.
- 32. Figures regarding Chinese casualties are still more difficult to obtain, but it is probable that the number is not far short of 850,000(') of all categories. The number of killed is tentatively put at 350,000. The almost complete absence of a Chinese Army Medical Corps has been the cause of the high percentage of "died from wounds or disease" in their casualty list. Their medical organisation is appalling, and very few seriously wounded Chinese soldiers ever reach base hospitals. In many cases wounded men have been known to walk over 100 kilom, before receiving any treatment other than very slight first aid in the front areas. The condition of these soldiers in the back areas is little better, where the men are to be seen roaming the streets dressed almost in rags, with bandages so dirty that open wounds have little hope of healing. Motor ambulances are insufficient, and many of the existing ones are put to uses other than those of transporting sick and wounded.
- 33. The China Red Cross under Dr. Robert Lim has done splendid work during the year, but his organisation is not on a large enough scale to permit of adequate facilities for the number of troops at the front.

Foreign Advisers.

34. During the latter part of 1938 the German Military Mission, headed by General von Falkenhausen, was withdrawn from China. Up to the time of their departure they had rendered valuable assistance, particularly in the preparation of the Hankow defences. They were not able, however, to obtain any executive powers from the Chinese army authorities, and much of their advice went unheeded. This, unfortunately, is a state of affairs usual in China, where advice is listened to but seldom acted upon.

Conclusions.

- (a) General.
- 35. The end of the year 1938 saw the Japanese in possession of considerable portions of Chahar, Suiyuan, and of many of the cities of Hopei, Shansi, Shantung, Kiangsu, Anhwei, Honan and Hupeh. Small areas in Kwangtung, Hunan, Chekiang and Fukien had also been occupied.
- 36. The pacification of these areas, however, is likely to prove a difficult task for the Japanese. The railways and main highways are under Japanese control, but the areas between are infested with guerrillas and bandits. This is true of the countryside within a few miles of such centres as Shanghai, Nanking, Wuhu and Tientsin.
 - (b) The Chinese Army.
- 37. Judged by Western standards the Chinese army has been reduced to a negligible factor. Chiang Kai-shek claims to have some 180 divisions still under his control, but the numerical strength of any such formation does not exceed 8,000 on paper, and it is unlikely that an effective strength of more than 5,000 all ranks is often passed. In addition to this, the armies of the generalissimo are almost entirely deficient in heavy artillery, very short of field and light artillery, and have but a small number of tanks. But the present war in China has shown that Western standards do not apply. Despite the overwhelming disadvantages
- (¹) These figures are taken from the War Office Intelligence Summary for November 1938 and represent the estimated casualties up to the end of October. Other less reliable estimates are considerably higher. For instance, General Itagaki, the Japanese Minister of War, is reported to have admitted in the course of an interview towards the end of 1938 that Japanese casualties were over 600,000 (including 200,000 killed), while the United States military intelligence is stated to estimate Japanese losses at between 700,000 and 800,000. As regards Chinese losses, General Chen Cheng, in a speech made in February 1939, stated that the Chinese army had suffered 1,200,000 casualties. In addition there were heavy civilian casualties on the Chinese side. An official report issued in Chungking in January 1939 gave the number of civilian casualties from air bombing alone between July 1937 and November 1938 as just under 80,000, including about 35,000 killed.

from which they have suffered it must be acknowledged that the Chinese armies have contained and inflicted very severe casualties upon Japanese forces numbering some 700,000 and equipped with all modern weapons and machinery. As regards mechanical transport, there would appear to be an adequate supply of lorries, but casualties amongst these vehicles are so numerous that a shortage is felt. In view, however, of the treatment to which all mechanical vehicles are subjected by the Chinese soldier driver, who cares little about maintenance and drives with abandon, it is doubtful whether anything but a very large importation of lorries will meet the needs of the forces in the field.

- 38. Since the fall of Canton, China has been severely handicapped by the paucity of road and rail communications from the coast to the interior. The only routes now remaining are via Pakhoi, and by the French Indo-China Railway from Hanoi to Kunming. Until recently, another route from Kwangchowan was available, but the threat of a Japanese landing at Pakhoi was enough to make the Chinese military authorities destroy the road. The threatened attack has not materialised, and all China has gained is a disruption of one of her few remaining lines of communication. The Yunnan-Burma road has been used for the transport of a certain amount of military stores, but traffic has been interfered with on more than one occasion by landslides.
- 39. From a review of all the factors, one can say with confidence that the Chinese can never hope to achieve a military victory in the field over their Japanese opponents. But what they can and do hope for is to be able by keeping their armies in the field and by active guerrilla tactics to contain the Japanese armies long enough to produce a state of exhaustion which will make impossible the continued prosecution of hostilities by Japan.

Air Operations.

40. During 1938 the number of Japanese military aircraft in China has shown a considerable increase, and this force is now backed by a fully-mobilised and efficient aircraft industry at home and an adequate supply and maintenance organisation. The approximate number of aircraft employed by the Japanese in the three major operations of the year were as follows:—

Lunghai railway operations	 	 	350
Yangtze Valley operations	 1	 	450
Canton operations	 	 	250

Although her growing air strength has been coupled with an increase in efficiency Japan cannot yet be considered a first-class air Power. Her air supremacy, to which must be attributed a considerable portion of her military success in China, has experienced no sustained opposition either in the air or from the ground.

- 41. The effective strength of the Chinese air force has been a variable factor during the year. It has been as low as 150 and has probably never exceeded 300 service aircraft. The absence of an aircraft industry in China and the consequent difficulties of maintenance and supply, allied with an initial insufficiency of aircraft and a shortage of trained personnel, have all combined to bring about the failure of the Chinese air force as an effective reply to Japanese air superiority. The failure of the Chinese to make effective use of their air resources can also be attributed to some extent to the Japanese offensive against all Chinese aerodromes from the opening of hostilities.
- 42. After the fall of Nanking in December 1937 the Chinese air force, now strengthened by Soviet aid, succeeded in re-establishing itself in the Nanchang-Hankow area. In February major operations were begun in North China along the Lunghai Railway; the Chinese, however, refused to throw the weight of their air force into this engagement, and air action was limited to reconnaissance and sporadic bombing by small formations. On the other hand, the Japanese concentrated a large number of aircraft in the north and, with no opposition in the air, these aircraft were able to play an important part in causing the eventual Chinese withdrawal from this area.
- 43. In June hostilities shifted to Central China along the Yangtze Valley. The Chinese air force, although inferior in numbers, had so far been able to maintain air superiority over the Nanchang-Hankow area, but with the move

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of the main enemy air strength to this sphere the initiative soon passed into the hands of the Japanese. During the operations against Hankow the Chinese managed for a short time to maintain an air offensive against the enemy land and river forces, but no attempt was made to counter the almost continual Japanese bombing attacks against the Chinese ground positions. The massed bombing tactics used so successfully by the Japanese during the Lunghai operations were again employed to an increasing extent until the fall of Hankow in October. The activity of the Chinese air force, despite the superiority of the Japanese air services, was maintained in this area until a month before the fall of Hankow, when that force, now largely composed of the Soviet air contingent, was immobilised. It was said at the time that the Russians withheld their machines by agreement with the Communists as a means of exerting pressure upon General Chiang Kai-shek to force him to defend Hankow at all costs. During the last two months of the year the Chinese air force, although withdrawn with little loss from Hankow and based on aerodromes in the southern and western provinces, undertook no active operations.

- 44. In the South China operations which brought about the fall of Canton in October the Japanese were entirely unopposed in the air. The Chinese stubbornly refused to split their air force over two fronts, even after the sustained and disastrous Japanese air attacks on Canton during May and June.
- 45. Since the occupation of Canton and Hankow the Japanese air services have not been extensively employed, and their activities have been limited to sporadic attacks on important cities, particularly in the southern and western provinces. Large civilian losses have been caused with no apparent effect on the conduct of hostilities.
- 46. The China National Aviation Corporation and Eurasia Aviation Corporation, by continually altering their routes and schedules, have managed to maintain their civil air lines over the territory still occupied by the Chinese. Although passenger aeroplanes of these companies have been attacked by Japanese military aircraft on three occasions, only one such engagement ended fatally, when an aircraft of the China National Aviation Corporation was shot down in Kwangtung with loss of life to passengers and crew.
- 47. The Japanese have inaugurated civil air lines in Chinese territory occupied by them, although such lines at present are being used only by military personnel. Japanese aviation firms have combined under the name of the Japan Air Transport Company to exploit these services, and have been subsidised by the Japanese Government in order to monopolise control of civil air services in the occupied areas of China when peace eventually comes.

(b) Unoccupied Areas.

Central Government.

- 48. The year opened with the headquarters of the National Government and the five Yuan established at Chungking with more important Ministries working in practice at Hankow and others dispersed to Changsha, Hengyang and Chungking, all operating under difficulties and with skeleton staffs. By degrees, as morale began to recover, the Ministries reassembled in Hankow. General Chiang Kai-shek also eventually established himself at Wuchang, and the Wuhan cities became in fact, though not in name, the capital of China.
- 49. As recorded in last year's report, the reorganisation of the Government after the outbreak of hostilities had led to confusion and overlapping of functions between the military and civil organisations. With the object of remedying this, a Government mandate was issued on the 1st January, 1938, introducing certain changes in organisation, of which the most important were General Chiang Kaishek's resignation from the post of president of the Executive Yuan in order to devote himself entirely to military affairs, and his replacement by Dr. H. H. Kung as president, with General Chang Chun as vice-president; the creation of a new Ministry of Economics, absorbing the Ministry of Industries, the National Economic Council, the National Reconstruction Commission and the Heavy Industries and War Economics Departments of the Military Affairs Commission; and the incorporation of the Ministry of Railways into the Ministry of Communications,

- 50. During the following weeks, further changes of detail were made and a new form of government eventually emerged which remained virtually unchanged for the rest of the year.
 - The military side of the Government consisted of:-
 - (a) A reorganised Military Affairs Commission, presided over by General Chiang Kai-shek, with Generals Yen Hsi-shan and Feng Yu-hsiang as vice-chairmen and General Chang Chun as secretary-general, and divided into four departments as follows:-

(1) Operations: General Hsu Ying-chang.

(2) Military Administration: General Ho Ying-chin.
(3) Military Training: General Pai Chung-hsi.
(4) Political: General Chen Cheng, with the Communist Chou En-lai as vice-director.

(b) Supreme War Council.

- (c) Advisory Council for National Defence, the membership of which had been increased with the object of making it the embodiment of the united front idea.
- 52. Of the above bodies (a) formed, so to speak, the executive side of the War-Time Government, while (b) and (c) were the legislative side. In addition, the old Military Advisory Council remained in existence principally for the purpose of enabling the Government to confer an empty compliment on military leaders.
- The civil side of the Government continued to function, although shorn of much of its authority, and was constituted as follows:-

Chairman of the National Government: Lin Sen.

Executive Yuan: Dr. H. H. Kung.

Legislative Yuan: Sun Fo.

Judicial Yuan: Chu Cheng. Examination Yuan: Tai Chi-tao.

Control Yuan: Yu Yu-jen.

The Executive Yuan consisted of seven Ministries:-

Ministry of Interior: Ho Chien.

Ministry for Foreign Affairs: Dr. Wang Chung-hui. Ministry of War: General Ho Ying-chin.

Ministry of Finance: Dr. H. H. Kung. Ministry of Economics: Dr. Oong Wen-hao. Ministry of Education: Mr. Chen Li-fu.

Ministry of Communications: Mr. Chang Chia-ngao.

There were, in addition, two commissions of Mongolian and Tibetan Affairs and of Overseas Chinese Affairs.

- Early in March Mme. Chiang Kai-shek resigned from the post of secretary-general of the Aeronautical Commission and Mr. T. V. Soong, at the pressing request of the generalissimo, took control of all air force matters.
- The principal object of the reorganisation was the preservation of national unity. The Kuomintang had not come through the trying months of the latter half of 1937 with credit, and the reorganisation involved a considerable weeding out of unsatisfactory members and an attempt to deal with corruption. In effect, since the period of political tutelage had not been brought to an end the Government remained a party Administration, but throughout the year little emphasis was placed on this fact and the Kuomintang remained as much as possible in the background, chief emphasis being placed upon the necessity for the united front of all factions. It is significant that the Central Political Council of the Kuomintang remained in abeyance throughout the year. Point was given to the united front idea by the incorporation of the Kwangsi leaders into the Administration, as exemplified in particular by the important posts given to General Pai Chung-hsi, who was Vice-Chief of the General Staff as well as Director of Military Training, and also in the important commands held throughout the year by General Li Tsung-jen. In particular, the members of the Advisory Council for National Defence had been so selected as to form a strong political Chiang-Soong-Kwangsi bloc. The third element to be brought into the

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Administration was the Communists, who secured representation in the person of Mao Tse-tung on the Advisory Council for National Defence and in that of Chou En-lai on the Military Affairs Commission; their chief influence was exerted behind the scenes rather than on the political stage and their incorporation into the Government, although successful, was not achieved without friction, caused primarily by the tendency of the Communists and the VIIIth Route Army in particular to pose as national saviours to the disparagement of the Kuomintang and the national armies.

56. The reorganisation of the Government also successfully brought about the clear demarcation of functions between the civil and military sides of the Government, which had been much obscured by the chaotic events of the preceding year, and achieved the important object of freeing General Chiang Kai-shek from administrative duties to enable him to devote his whole energies to the organisa-

tion of national defence.

57. General Chiang Kai-shek's influence was further strengthened as a result of the Extraordinary National Congress of Kuomintang delegates which was convened at Hankow at the end of March. One of the principal decisions taken was the conferment upon General Chiang Kai-shek of the title of Tsung Tsai, or General Executive, with Mr. Wang Ching-wei as his deputy. The effect of this was to give the generalissimo the right to act as chairman of the National Kuomintang Congresses and of the Central Executive Committee, and to veto the decisions of either body. As he already controlled the military machine in his capacity as chairman of the Military Affairs Commission, and the War-Time Government in his capacity as chairman of the Supreme War Council, he obtained in effect dictatorial powers and was accepted henceforth without question by all parties as the acknowledged leader of the country in its resistance to Japan.

58. A manifesto issued by the Kuomintang Congress emphasised the determination of the country to continue resistance and stressed the necessity, nevertheless, of not allowing economic development to be delayed by the war. A further result of the congress was the reaffirmation of Kuomintang principles and the general purification of the party. The congress was immediately followed by meetings of the Fifth Central Executive Committee and the Fifth Central Supervisory Committee, as a result of which considerable changes in party per-

sonnel were made.

59. One of the most important acts of the congress was the creation of a National People's Political Council, which was eventually made up of 200 members chosen as to one-half from representatives of the Provincial and Municipal Governments and from the political parties, and as to the other half from persons who had served with distinction in cultural and economic spheres or had rendered outstanding services to the State. Mr. Wang Ching-wei was appointed president of the Assembly, Mr. Chang Po-ling (president of Nankai University, Tientsin), vice-president, and Dr. Wang Shih-chieh (formerly Minister of Education) secretary-general.

60. The first session of the assembly took place in Hankow in the second week of July. The list of members was representative, including, besides nearly all the intellectual leaders of the country, representatives of most of the occupied areas and of the overseas Chinese, and also six Communists. A preparatory step to the admission of Communists to the assembly had already been taken on the 3rd June when the Central Supervisory Committee of the Kuomintang decided to readmit to membership of the party twenty-six former members who had been expelled for political reasons. Among those who benefited by this decision were General Mao Tse-tung, the well-known Communist leader, Chou En-lai, the resident representative in Hankow of the Chinese Communist party in the northwest, and Eugene Chen, the former Minister for Foreign Affairs.

61. The proceedings of the assembly were marked by considerable criticism of the Government, but on the vital question of support for the generalissimo in the anti-Japanese campaign and the maintenance of the united front there was complete unanimity amongst all groups, which was expressed in a manifesto issued at the closing session. On the departure of the members of the assembly from Hankow, its affairs were left in charge of a standing committee of

twenty-five.

62. The succeeding months were marked by considerable activity behind the scenes on the part of the Communists and by differences of opinion, which were

prevented, however, from developing into an open breach between them and the generalissimo on the question of defence of Hankow. As the Japanese advance up the Yangtze proceeded, Government departments were evacuated up-river to Chungking, some of the more important Ministers remaining, however, in Hankow. with the generalissimo and the military leaders, until the last moment.

- 63. The occupation of Hankow was quickly followed by a further session of the National People's Political Council. This was to have been held in mid-September. The reason given for its postponement was the difficulty of transport, but the generalissimo's desire to avoid bringing to a head the friction between the Communists and the Right elements in the Kuomintang probably contributed to the decision. When it eventually met at Chungking in the last week of October and the first week of November, its deliberations on questions of national policy revealed a tendency to divide into a pro-Russian group headed by Dr. Sun Fo, a second group which continued to rely on the support of democratic Powers in a common cause, and a third which held that the conclusion of an early peace should be the foremost aim. Before closing its session the council was prevailed upon to leave questions of foreign policy to the Government for the time being, and passed a resolution, with one dissentient vote, supporting the Government's policy of armed resistance against Japan.
- 64. A further contribution to the general recovery of morale after the reverses of Canton and Hankow was made by the generalissimo, who issued a message of encouragement to the nation on the 31st October during the session of the Congress. Timely support was also forthcoming from the Chinese Communist party, who, on the 23rd November, published a manifesto, based on resolutions adopted earlier in the month by the Central Executive Committee of the party at its headquarters at Yenan in Shensi, reaffirming the party's pledges of support for Chiang Kai-shek and the Kuomintang Government and the policy of resistance to Japan, and requesting permission for Communists to join the Kuomintang and the Youth Corps, which had been created at the time of the Kuomintang Congress at the end of March with the task of instilling the spirit of the Three People's Principles into the youth of the country.
- 65. Persistent rumours regarding the activities of the so-called peace party, the third group which emerged during the two sessions of the National People's Political Assembly, came to a head towards the end of December, when Mr. Wang Ching-wei departed suddenly from Chungking and issued a message from Hanoi advising General Chiang Kai-shek to enter into peace negotiations on the basis of the statement made by Prince Konoye on the 22nd December. On the 26th December General Chiang Kai-shek, in a long speech at the weekly memorial meeting at Chungking, criticised the recently declared Japanese policy of a new order in East Asia, and announced that Prince Konoye's statement could not possibly be considered a suitable basis for peace negotiations. The ground was further cut from under Mr. Wang Ching-wei's feet by the decision taken at a special meeting of the Central Executive Committee and the Kuomintang on the 31st December expelling him from the party and depriving him of all his posts.
- 66. The year accordingly closed with the Government as closely united as ever before and undoubtedly enjoying the support of the overwhelming majority of the people of China. It is no small tribute to General Chiang Kai-shek's statesmanship that national unity should have been so successfully maintained and the processes of Government so successfully reorganised in face of the immense difficulties which confronted his Administration during the year.

Provincial Governments.

67. The developments of the past year have thrown the Central Government into closer contact than ever before with the notoriously independent provinces of the south-west, and, although many problems concerning local autonomy undoubtedly remain to be solved in Szechuan, Yunnan, Kweichow, Kwangsi, Kwangtung and Fukien, latent jealousies have been successfully concealed and a surprising degree of unity maintained. Provincial troops have been employed far from their homes, and the feeling that they are fighting in a common national cause has undoubtedly taken a strong hold. Moreover, the presence in the south-

west of Central Government forces, the improvement of communications, the introduction of a national currency and the establishment of Central Government offices and banks have all contributed to breaking down the particularism of the past.

- This influence was probably strongest in Szechuan. Here the issue was precipitated by the death on the 20th January of General Liu Hsiang, who for many years had been chairman of the province. The Central Government seized the opportunity to appoint General Chang Chun, the vice-chairman of the Executive Yuan and a Szechuanese, to the vacancy, but the appointment immediately aroused opposition and the general did not proceed to his post. The difficulties were temporarily overcome by leaving the chairmanship in abeyance and appointing one of the Szechuanese generals as Pacification Commissioner, and in May General Wang Tsan-hsu, a disciple of the late General Liu Hsiang, was appointed acting chairman. On the 1st August General Chang Chun resigned his post of chairman and was appointed director of the Chungking Provisional Headquarters of the president of the Military Affairs Commission, in which capacity he was able to proceed to Chungking, while General Wang Tsan-hsu received the substantive post of chairman. Meanwhile, General Liu Wen-hui, the uncle and erstwhile rival of General Liu Hsiang and his henchman, and the chief opponent of Central Government penetration in the province, was being kept busy at a safe distance in the border territory of Sikang. By such face-saving expedients provincial prejudice was successfully overcome, and the province has been ardent in its protestations of loyalty to the Central Government in the common cause. After the fall of Hankow the Szechuan generals telegraphed to General Chiang Kai-shek assuring him of their continued support. In November there was some local armed opposition to corrupt recruiting methods, but this was successfully dealt with, and at the end of the year the province's pledges of solidarity were apparently being fulfilled.
- 69. In Yunnan also particularist tendencies are being gradually overcome. The old-established provincial chairman, General Lung Yun, has declared his loyalty to General Chiang Kai-shek and sent him a message of support after the fall of Hankow. Although sceptics expressed doubts whether they would be employed outside the borders of the province, considerable numbers of Yunnanese troops were recruited and trained during the year and employed as far afield as Fukien. Moreover, the provincial authorities have realised the value of co-operation with the Central Government in developing the natural resources of the province and in opening up communications. Although many enterprises have been established under local control, the National Resources Commission and the Foreign Trade Commission have been allowed to play their part, while successful efforts have been made to extend the use of the national currency, which was already established in the neighbouring province of Kweichow.
- 70. In Kwangsi again, despite persistent rumours of differences between the local leaders and General Chiang Kai-shek, provincial loyalty appears to have been successfully retained, and, although the province has developed in recent years on independent, authoritarian Socialist lines and its natural allegiance still tends to be to Generals Li Tsung-jen and Pai Chung-hsi, there appears to be no doubt of the personal loyalty of these leaders.
- 71. If in Kwangtung there was some disloyalty it is because this province was far more vulnerable and open to outside subversive influences. Early in February a plot, engineered by Japanese, for the overthrow of the Provincial Government was discovered in the nick of time. Japanese efforts continued, however, and, apart from the distribution of bribes, they doubtless relied also on their ruthless bombing of Canton to shake the province's allegiance to Hankow. The air attacks defeated their own object, but that "silver bullets" were not without effect was the conclusion drawn by many observers from the capitulation of Canton in October. The full story will probably never be known, but the collapse of Kwangtung's resistance after the Japanese landing at Bias Bay suggested, to say the very least, a serious lack of co-ordination between the Provincial and Central Governments and to the latter it came as a genuine surprise. The effects of the shock did not last long, however, and relations now appear to have been to some extent adjusted with the confirmation in office of the provincial chairman,

General Wu Teh-chen, who had reappeared in the northern part of the province, at the end of October and reaffirmed his allegiance to the Central Government and the cause of prolonged resistance.

72. The position in Fukien is also far from clear. The fact that, despite persistent rumours of impending descents on the coast and the removal of all the Provincial Government offices from Foochow, the Japanese have made no attempt at military occupation of the province beyond the seizure of the island of Amoy in May by a Japanese naval landing party, suggests to some that other methods are being tried of winning it over. There is, however, no direct evidence to support this supposition, and local information insists that the provincial authorities remain loyal to the Central Government. It seems likely that the latter have their suspicions of the chairman, General Chen Yi, for, while approving his energy in developing the province, they have been careful to retain control of policy by garrisoning the province with troops from Chekiang and Yunnan under the command of a Chekiang general.

(c) Occupied Areas.

Administrations sponsored by Japan.

- 73. During the year Japan's administrative policy in those parts of China which she claims to have occupied has gradually taken shape. Everywhere the pretence has been made of setting up Chinese administrations and all intention of annexation has been repudiated. The real power, needless to say, remains with the Japanese military authorities, but care is everywhere taken to create the impression that the Chinese are governing themselves. The first step has always been the establishment of local administrations to assist the Japanese forces of occupation in the policing and later the general administration of the occupied district. Thus, on the occupation of Tsingtao by the Japanese navy in January, a Peace Maintenance Committee was immediately set up under a Chinese chairman, and Chinese police began to appear on the streets. Similar measures were taken in Chefoo, where the Chinese puppet received on the 4th February the highsounding title of chairman of the East Shantung Rehabilitation Office with jurisdiction in theory over thirty-two districts, and, in his concurrent capacity as Mayor of Chefoo, with administrative authority over the municipalities of Lungkow and Weihaiwei as well as Chefoo. This unfortunate man's titles were more than usually empty since, apart from the fact that he was surrounded by Japanese "advisers," the towns he ruled remained completely isolated from one another throughout the year, Japanese military authority extending only a few miles into the surrounding country in each place.
- 74. As the Japanese advance progressed up the Yangtze, attempts were again made to organise local Chinese administrations. The capture of Amoy Island in May was followed by the establishment there of a Committee for the Preservation of Law and Order, pending the setting up of a municipal government. Similar steps followed the occupation of Hankow and Canton. In Hankow a body known as the Wuhan Peace Maintenance Association made its appearance on the 25th November, while in Canton the Kwangtung Peace Maintenance Commission was inaugurated on the 20th December. Neither of these two bodies appears to have any real authority, and it is doubtful whether the Japanese themselves set much store by them. Like similar organisations elsewhere they suffer from the usual inability of the Japanese to find reputable Chinese to fill the rôle of puppets.
- 75. In North and Central China such local administrations are co-ordinated in theory under the authority of the "Provisional Government of the Republic of China" at Peking and the "Reformed Government of the Republic of China" at Nanking.
- 76. The inauguration of the Peking Provisional Government on the 14th December, 1937, was recorded in last year's report. In accordance with the announcement made immediately after the establishment of the new Government, the East Hopei Anti-Communist Autonomous Government was dissolved by the signature of an agreement of the 30th January, whereby the Peking Government took over its functions. The difficult problem of its actual liquidation was

not, however, completely disposed of until some time later. The Chinese municipalities of Tientsin and Peking were at the same time reconstituted into Special Municipal Administrations.

- 77. The Peking Government adopted the organic principles of the Central Chinese Government. It consisted of three Commissions: Executive, Legislative and Judicial, obviously a modified form of the five-Yuan system. The Executive Commission originally embraced five dependent ministries, besides a secretariat. These did not include portfolios of foreign affairs or war. A Ministry of Industry was created in May, and Ministries of Finance and the Interior in October. Foreign affairs were dealt with in theory by the appropriate bureau of the Ministry of Administration, but in practice—in so far as they existed at all—by the Japanese Special Military Mission under General Kita, the principal creator of the new Government. Military affairs, it was announced, would be looked after by the Japanese army, and the only forces at the disposal of the Government are the village militia, who are normally armed only with staves and are kept under strict Japanese supervision.
- 78. The Chinese officials of the Peking Government are either returned students from Japan or elderly survivors of the pro-Japanese Anfu and Chihli parties. All the ministries are heavily staffed with Japanese advisers. The only outstanding man is the president of the Executive Commission, Mr. Wang Keh-min, who, in the absence of any head of the State, was the leader of the Government. He was considered of sufficient importance for an attempt to be made on his life in March. Although enjoying the confidence of General Kita, he was considered too independent by less liberal Japanese, such as General Terauchi, the Commander-in-chief in North China, who transferred his head-quarters to Peking in January.
- 79. The legislative activities of the Government were principally of an ad hoc character, designed to meet emergency conditions arising out of the hostilities. The existing legal system inherited from the National Government was taken over, except where revision or amendment was called for in the interests of "public order," in other words, the campaign against Communists and guerrillas. An important and retrograde measure, presumably prompted by these considerations, was the repeal of the National Government's comprehensive land legislation. Little attempt was made to change the existing arrangements for raising revenue, which was one of the Government's principal preoccupations, the existing machinery for the collection of taxes and customs duties and for the administration of posts and telegraphs having been taken over wherever possible and the receipts eked out by special expedients, such as the encouragement of opium-smoking under official control.
- 80. The Nanking Reformed Government was inaugurated on the 28th March. In organisation and personnel it was the exact counterpart of the Peking Provisional Government, except that, unlike the former, it contained a number of Kwangtung and Fukien men. Like the Northern régime, it was the creation of the Japanese army, and, indeed, for the first few months of office the members of the Government remained in Shanghai under the eye of their masters, the Japanese Army Special Service Section. This Government's achievements appear to have been even less noteworthy than those of the Peking Government, their subservience even greater and their financial difficulties an even more serious handicap. Above all, they have tended to be overshadowed by and in permanent dispute with a rival puppet Administration in Shanghai, which is nominally subservient to Nanking. As originally constituted in December 1937, the Shanghai régime was known as the "Ta Tao," or "Great Way" Administration. On the 28th April, 1938, it was transformed into the Greater Shanghai Municipal Government. The head of both these régimes was a Chinese Buddhist scholar from Tokyo, called Su Hsi-wen, who was persuaded to accept the post as the nominee of the Japanese naval landing party. The rivalry between Nanking and Shanghai and their squabbles over the destination of funds and perquisites were accordingly merely a reflexion of the perpetual struggle between the Japanese military and naval authorities. In October the former appeared to have gained the upper hand with the relegation of Mr. Su Hsi-wen to the post of secretary-general and the installation as mayor of a reorganised and extended municipal administration of Mr. Fu Siao-an, a

well-known Shanghai commercial magnate, who owed his appointment to General Doihara and the Special Service Section of the Japanese army. Mr. Fu is reported to be *persona grata* with the Nanking Reformed Government, and the former disputes have now given way to internal dissension in the Shanghai Administration, where Mr. Su Hsi-wen is using his new position to obstruct the processes of government.

81. There has naturally been violent criticism among loyal Chinese of the action of those who have accepted office under the orders of Japan, and numerous attempts were made to assassinate those suspected of harbouring such intentions. Nevertheless, while most of the puppets are pure office-seekers, a few have probably been prompted by the thought that in assisting in the establishment of any Administration, even under Japanese auspices, they were contributing to the welfare of the Chinese population, whom they regarded as having been deserted by the Kuomintang régime. The latter, they claimed, had deliberately destroyed the people's means of livelihood in pursuance of the scorched earth policy and had then fled, leaving the people to fend for themselves and to face the wrath of the exasperated invaders.

The inaugural declarations of both the Peking and the Nanking Governments had each emphasised the need for reconstruction. It was soon made clear, however, that reconstruction was to be primarily in the interests of Japan and in accordance with Japanese ideas. This was particularly so in the north. There the chief instrument for the moulding of the lives and opinions of the Chinese after approved Japanese models was the Hsinminhui, or New People's Association, which was set up in Peking on the 24th December, 1937. Branches were later established in Tientsin, Tsinan and other centres. This organisation was extremely active during the year under Japanese guidance. It was the chief organ for the strict control of the press and the supervision of education. It established an "East Asia Cultural Association" and an academy for the training of civil servants, it sponsored a youth training institute and an athletic commission, it organised a labour union in Peking, and it directed a co-operative movement in the country districts. Its aims were declared to be opposition to the Comintern and the Kuomintang, support for the new régime, friendship and co-operation with Japan, improvement of the livelihood of the people and the promotion of morality and culture on the basis of the old Chinese sages and in accordance with the precepts of the "Kingly Way," a political doctrine of Japanese manufacture which has already played an important part in the early development of Manchukuo. Indeed, the methods adopted in North China offer a strikingly close parallel to those which have been used further north, and it is no doubt intended that the Hsinminhui shall become in time, like the Concordia Society of Manchukuo, the single "national" party supporting a totalitarian Government, and membership thereof the sole sure guarantee of respectability and eligibility for public office. While the Hsinminhui's activities have not so far been extended to Central China, the Japanese authorities in Nanking and Shanghai have devoted considerable energy towards the foundation of various secret societies and political organisations designed to spread pro-Japanese propaganda and to cater for the spiritual needs of the masses. The least disreputable of these organisations and that which offers the closest analogy to the Hsinminhui is perhaps that known as the Taminhui, or Great People's Society.

83. The establishment of closer relations between the Peking and Nanking Governments has been aimed at from the beginning. At the time of its inauguration the Peking régime announced that it was a Government of all China, and that as such it would seek the recognition of foreign Powers and would assume all foreign obligations which had been publicly contracted by previous Administrations. The Nanking Government was careful to explain that it was a temporary institution which would be amalgamated with Peking as soon as communications were restored on the Tientsin–Pukow and Lunghai Railways. Discussions with a view to amalgamation took place in May, but led to nothing, since control was not established as quickly as had been expected over the country lying between the two capitals. By September the original plans had to be revised, and as a temporary expedient a "Joint Commission" of the two Administrations was inaugurated in Peking on the 22nd of that month, with Mr. Wang Keh-min

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as chairman. This step was the outcome of a conference arranged at Dairen between Mr. Wang Keh-min and Mr. Liang Hung-chih, the president of the Executive Commission of the Nanking Government. It was accompanied by the issue of a manifesto denouncing General Chiang Kai-shek as an enemy of the Chinese people. After the fall of Hankow efforts to amalgamate the two Governments were redoubled, and at the second meeting of the Joint Commission, which was held in Nanking at the end of October, plans were discussed for the formation of a federation of the occupied areas. These schemes were defeated, however, by the rivalries and conflicting views prevailing in Japanese military circles, and by the difficulty of finding a suitable candidate for the post of provisional president of the federation. Attempts to induce the veteran statesman, Mr. Tong Shao-yi, to accept such a position had led to his assassination at the end of September. In December there seemed to be a chance that General Doihara's attempts to induce Marshal Wu Pei-fu to emerge from his seclusion in Peking might at last be successful. But shortly before the end of the year it became known that the marshal had categorically rejected the proposals which had been made to him—according to reports, he was standing out for a considerable army of his own—and the dreams of the Japanese were apparently as far as ever from fulfilment.

Administrations sponsored by the Chinese Government.

84. Although the Japanese have established the machinery of government in the occupied areas, they have scarcely begun the task of administering the country. It is no exaggeration to say that at the end of the year they still held merely points and lines. All the principal towns in the occupied areas were theirs, with the railways connecting them, some of the main roads and the Yangtze River as far as the Tungting Lake. Over the rest of the country they had no control. Thus it was that in November the Chinese were able to claim that, in the nine provinces affected by the hostilities, by the beginning of October the Japanese at that time exercised complete authority over only 7·41 per cent. of the hsien districts outside the big municipalities, while 61·44 per cent. were under the complete control of the Chinese Central Government, and 31·15 per cent. under their partial control. There is no reason to consider these figures greatly exaggerated.

85. It is in North China that the most striking progress has been made by the Chinese in consolidating their hold over the country behind the Japanese advance. Here at the beginning of the year conditions were chaotic. With the retreat of the Chinese armies towards the south-west in the autumn of 1937 the Administration had broken down. In the villages local mobilisation committees had been set up, primarily as a defence against bandits, but there was no larger organisation. It was under these conditions that, as a result of consultations between the civil and military leaders of the area and Generals Yen Hsi-shan of Shensi and Chu Teh of the Red Army, a conference met at Fuping in Shansi on the 10th January. This meeting of representatives of thirtynine hsien selected a committee of nine to form a Government, which received the approval of General Chiang Kai-shek on the 22nd January, and that of the Executive Yuan of the Central Government on the 1st February.

86. The governing committee included adherents of the Communist party, the Kuomintang, and of General Yen Hsi-shan's Hsinmenghui. Their average age was 34. Some were veteran army commanders and some former newspaper editors or provincial officials. After establishing its headquarters in Shansi this Government next devoted its attention to the districts of Central Hopei to the east of the Peking-Hankow Railway, and on the 1st April a Central Hopei Government was formally inaugurated as part of the joint Border Government of Hopei-Chahar-Shansi. On the 9th March a Civil Governor, General Lu Chung-lin, appointed by the Central Government, arrived in Hopei and established his provisional capital at Nankung. By August the Border Government was reported to control an area of 95,000 square miles with a population of about 45 million. The area consisted of about twenty-eight hsien in Central Hopei, fourteen in West Hopei, fourteen in North-East Shansi and three in South Chahar. It was divided into two halves by the Peking-Hankow Railway,

of which the Japanese retained control. During the latter half of the year the penetration of East Hopei was begun. This area had been under Japanese rule since the establishment of the Chitung Administration in 1935, and the Chinese had a hard struggle to gain control. Although little effective administration had been set up in this area, the Chinese claimed, nevertheless, to have penetrated seven hsien and to have established contact with guerrillas in Manchuria.

- 87. The Border Government, although owing much to the experience and efforts of the VIIIth Route Army in Shansi, is organised on a basis of non-party nationalism which aims at achieving a united resistance against Japan. This resistance is organised on three fronts, political, economic and military.
- Political organisation came first. Magistrates, mostly young men under 30, were appointed by the Government to replace the puppets set up by the Japanese in the course of their advance and to organise the local administration. The village mobilisation committees were abolished as normal administration was restored. Considerable improvement took place in provincial and hsien administration, but this had not by the end of the year been matched in the villages. Attempts were being made, however, to fill the gap caused by the abolition of the village mobilisation committees by encouraging the growth of bodies such as the Farmers' Union, the Workers' Union, the Women's Association and the Youth Association. Considerable attention was devoted to education both in the schools and through a mass movement, emphasis being given to anti-Japanese propaganda rather than to the inculcation of party principles. Postal and telephone services were also restored. By the end of the year it was probably true to say that the areas under the control of the Border Government were enjoying administration as good as any they had ever received before and the foundations had been laid for permanent resistance to Japanese penetration of the local administration system.
- 89. In the economic sphere the principal aim of the Border Government has been to prevent the Japanese from deriving any economic profit from North China. Attempts are being made to reduce to the minimum trade between the Japanesecontrolled and the Chinese-controlled areas. The peasantry in the Chinesecontrolled districts are to a considerable extent self-supporting and the Chinese authorities are in a position to exert considerable pressure on the Japanese by means such as the replacement of cotton and similar export crops by food crops which can be consumed locally. Much progress has also been made in the unification of taxes and the reduction of rents and interest rates. The Government has also issued its own currency and has floated an internal loan. There has been some criticism of the Government's policy on the part of the landlords and gentry, but the authorities disclaim Communist principles, and emphasise the importance of preserving the united front, not only in the political sphere by encouraging good relations between the army and the people, and between the civil and military officials, but also in the economic sphere by preventing the excessive bleeding of any one class and by eliminating political corruption. All officials are content with very low salaries, the highest pay for a district magistrate being eighteen local dollars a month.
- 90. The military activities of the Border Government are those which receive most publicity, but are certainly not more important than the work in the political and economic spheres, which is laying the foundations of a new social system in North China and of a new national consciousness among the peasants. In the military field the authorities have concentrated on restricting the Japanese to the large towns and the railways and they have been uniformly successful. Their continued attempts to disrupt the Japanese lines of communication have not had more than a nuisance value, although the recurrent dislocation of traffic on the various railways has been a source of worry to the Japanese and has obliged them to maintain considerable garrisons all along the railways.
- 91. While the Chinese activities behind the lines are nowhere else as highly organised as in the territory of the Border Government, guerrilla activities, supported by various degrees of political organisation, are widespread. In South Shansi and Northern Honan a mixed force of VIIIth Route Army, Central Government and Provincial Government troops are operating. In

Shantung also large numbers of guerrillas have successfully restricted the Japanese to the coast ports and a few large towns, such as Tsinan. The Chinese claim that in Shantung the Japanese have not complete control of a single hsien outside these centres, while the Japanese themselves have admitted that they only have influence in thirty-six out of the 108 hsien in the province. A Civil Governor appointed by the Central Government is functioning in Shantung as in Hopei, and it is reported that a Hopei-Honan-Shantung Border Government is being formed. In Kiangsu, Anhwei and Chekiang guerrilla activities have also been continued by Chinese troops left behind the Japanese lines when the main body of the Chinese army retreated. Efforts are being made to organise these guerrillas into a new IVth Route Army under the control of the Central Government. Finally, in Kwangtung, guerrillas have harassed the Japanese since their occupation of Canton.

92. Since the fall of Canton and Hankow and the halt in the Japanese advance, the Chinese Central Government have had time to devote their attention to the organisation of these political and military activities behind the Japanese lines, and had by the end of the year adopted it as their deliberate policy. As time goes on, it is likely that a greater degree of co-ordination will be brought about, and that, by consolidating their hold over the country before the Japanese have had a chance of doing so, they will bring about a state of affairs which will render the Japanese control increasingly precarious and make anything like a permanent occupation out of the question unless the Japanese are prepared to keep immense forces in China on active service indefinitely. In some districts the disturbed conditions have led to a serious increase in banditry pure and simple, especially in the no-man's-land between the Chinese-controlled areas and the Japanese lines of communication. There has been evidence of the encouragement of such activities by the Japanese in order to discredit the guerrillas with the population. While banditry will no doubt be brought under control eventually, it is evident that, even at the best, conditions in many areas will remain chaotic for years, and that meanwhile the outlook will not be encouraging for the foreign trader or traveller.

(d) Mongolia.

- 93. There were no political developments of importance in Inner Mongolia during the year, which was a period of consolidation in the political and economic fields. The supreme political authority in the area continued to be the Mongolian Frontier Joint Commission, which, as recorded in last year's report, had been set up on the 22nd November, 1937, at Kalgan as a sort of federal organ embracing the three constituent puppet Administrations: the South Chahar Autonomous Government with its capital at Kalgan, the North Shansi Autonomous Government with its capital at Tatung, and the more recently established Mongolian Federated Autonomous Government with its capital at Kweihua (renamed Houho) in Suiyuan. The aim of the Japanese in thus associating their new puppet in Suiyuan with the two more proven ones in Chahar and Shansi appears to have been to reduce the effective autonomy of the Mongols of Inner Mongolia and to reduce to the minimum their associations with their Soviet-controlled brethren of Outer Mongolia. In this they appear to have been relatively successful, and relations between the two Mongolias were, so far as can be ascertained, confined to the usual frontier raids and nomadic comings and goings over the border.
- 94. In July the Kweihua Government inaugurated a so-called Third Mongolian Congress at their capital. The first two congresses were apparently those which met at Ujumuchin in April 1936 and Kalgan in October 1937 respectively. The principal business of the third congress was the election of Prince Te (Teh Wang) as chairman and General Li Shou-hsin, the Commander-in-chief of the Mongolian army, as vice-chairman of the Mongolian Federated Autonomous Government. The original chairman, the septuagenarian Prince Yun, had died in March.
- 95. The real power in the land is the Kwantung Army. It is they who have been responsible for the policy of fostering the independent existence of the "Meng Chiang Federation," which is gradually achieving a separate entity comparable to that of Manchukuo. It is rumoured that this development was at first

by no means welcome to the Japanese sponsors of the Peking Provisional Government who had hoped to see all of the five northern provinces of Shantung, Hopei, Chahar, Shansi and Suiyuan come within their sphere. In consequence, the Inner Mongolian régime's relations have been closer with Hsinking than with Peking and the exchange of goodwill missions with Manchukuo and with Japan was arranged during the year.

- 96. The Kwantung Army, however, laid the chief emphasis during 1938 on cultural and economic development. In the first sphere plans were made for the establishment of Mongol colleges in the territories of each of the three autonomous Governments. Each Government was also to have its official newspaper, controlled by an institution to be set up as part of the Mongolian Frontier Joint Commission's three-year development plan "to impart to the 7 million inhabitants of the new State all news regarding pacification, politics, education and other matters." This institution is also reported to have decided to produce and show Mongolian cinema films and to operate a modern printing press. The vigour with which such means of propaganda are being pushed is a measure of the importance attached by the Japanese to countering Soviet cultural penetration from Outer Mongolia and is essential to the fulfilment of the Kwantung Army's traditional policy of the creation of a buffer State between the Soviet Union and their sphere of influence in North China.
- 97. In the economic sphere, too, the Inner Mongolian State has been encouraged to pursue a line of its own, although the Kwantung Army may find it difficult as time goes on to resist the absorption of Inner Mongolia in a Manchukuo-Mongolia-North China economic bloc. But, for the time being at least, the Japanese on the spot enjoy complete control of economic affairs. Capital development in Kalgan and the construction of highways in the interior is being encouraged with Japanese enterprise and materials. The Meng Chiang Bank established at the end of 1937 and operated under Japanese management has a complete monopoly of all financial business and enables the authorities to maintain an effective control over currency and the export of bullion. By their military control of the Peking-Suiyuan Railway, the main artery of the new State, the Japanese exercise a monopoly over practically all trade, in particular the important exports of animal furs and skins. Moreover, in Suiyuan, which, with Jehol, is the chief source of supply of opium in North China, the Japanese military authorities have established a purchasing monopoly of raw opium, which renders handsome returns and has sent up the price of opium so high as greatly to increase its cultivation. On the other hand, attempts to introduce monopolies of the distribution of cigarettes and petroleum products failed and were abandoned, after representations had been made by His Majesty's Embassy at Tokyo.
- 98. Some observers have reported that Japanese control is leading to a stagnation of trade in Inner Mongolia and to the diversion westwards to the Union of Soviet Socialist Republics or Central China of the products of Mongolia, Kansu and neighbouring regions which formerly found an outlet through Kalgan and Tientsin. However that may be, the Japanese hold over the country is far from complete. The railway has been kept open without difficulty by very small garrisons, but in the outlying districts conditions have been unsettled. There has, however, been little sign of organised guerrilla activity such as has been carried on in Hopei, and such difficulties as the Japanese have encountered have probably been due to the haphazard operations of bandits and of remnants of the Chinese North-Western Armies, supported by disaffected Mongols.

(e) Sinkiang.

99. It was recorded in last year's report that the resumption of control by the Provincial Government over Southern Sinkiang after the collapse of the Tungan Rebellion had been accompanied by a vindictive policy on the part of officials towards British traders. At the end of the year this attitude developed into a virulent anti-British boycott, which was actively fostered by the police and military authorities. In Kashgar the deterioration coincided with the departure of the District Administrative Commissioner, Mr. Wang Hsien-ting, for Urumchi early in December 1937, but it appears to have been part of a deliberately organised outbreak which extended all over Sinkiang. It may have had some

connexion with the arrival of a new Soviet Consul-General at Urumchi. The pretext for the outbreak was the widely held belief that the Tungan rebellion could not have taken place without support from India. Proof of the Government of India's sympathy with the rebellion was seen in their failure, in the absence of any extradition treaty, to hand over to the Provincial Government either the rebels, Mahmud Shih-chang and Ma Hu-shan, or, what was doubtless still more important, the considerable quantity of gold which the latter had taken with him in his flight. In any case, the Russians were doubtless quick to appreciate the cover for their own activities provided by the anti-British outburst, and it was probably from Soviet quarters that the current rumour emanated that the Tungan rebellion had been engineered by Japanese acting through India. Efforts to couple Great Britain and Japan in the popular mind as the two archenemies appear, indeed, to have been persistent and not unsuccessful.

100. Soviet Russia seems to have regained in full the influence Imperial Russia used to exercise in Sinkiang. The process of centralisation in the province has reached its peak; nothing can be settled without reference to Urumchi, and the Soviet Consulate-General there is now superior to that at Kashgar. Relations between the Provincial Government and the Chinese Central Government are correspondingly tenuous. The Provincial Government, while resenting any interference from the Central Government, accepts such of the latter's rulings as prove likely to be useful. An example is the business tax, loosely based on regulations promulgated by the Central Government, by which it is hoped eventually to replace various vexatious impositions hitherto in existence.

101. On the whole, administration has improved with the extension of Urumchi's control. Except for a mutiny of Kirghiz troops in Kashgar and its neighbourhood in July, conditions have been relatively quiet. Despite the introduction into South Sinkiang of the system of secret police on the Soviet model, which has existed for some years in the north, the people are more secure than hitherto, and attention is being devoted to education and the improvement of communications.

In Kashgar the power in the land during the year has been General Chiang Yu-fen, the Kashgar garrison commander, who, on instructions from Urumchi, took over Mr. Wang Hsien-ting's functions as Administrative Commissioner on the 15th January. On the 24th January His Majesty's Consul-General presented an official note to him designed to disabuse the local authorities of their suspicions regarding the attitude of the Government of India and His Majesty's Consulate-General, and protesting against the virtual boycott of British subjects throughout the province, which had even been extended in some measure to the consulate-general. This note produced no improvement in the situation, and in March merely called forth a denial that there had been any anti-British activity. Representations by His Majesty's Ambassador to the Chinese Central Government having made it clear that, while they would not admit it, they had no control over Sinkiang, and a visit to Urumchi by a member of the staff of His Majesty's Consulate-General at Kashgar being for various reasons impracticable, it was decided to allow a secretary from His Majesty's Embassy at Moscow to make the attempt to reach Urumchi and endeavour to obtain an improvement in the situation. Mr. F. H. R. Maclean accordingly left Moscow on the 6th June, having been furnished with an exit visa by the Soviet Government and a visa and a laissez-passer by the Chinese Central Government, who also sent instructions to the Sinkiang Government to afford him all possible facilities. On arrival at the frontier, however, he was met with a categorical refusal on the part of the provincial authorities to allow him to enter, and he was obliged to return to Moscow. His Majesty's Ambassador at Moscow had no hesitation in attributing this unfriendly attitude to Soviet influence, direct or indirect.

103. Meanwhile, the boycott of British traders and the unhelpful attitude of the local authorities towards His Majesty's Consulate-General continued. In June there was a slight improvement, and, at least, the serious interference with couriers carrying official British mails was stopped. In July, however, there was a recrudescence of police persecution of local persons having dealings with His Majesty's Consulate-General, and this continued in succeeding months. Considerable difficulty was experienced in obtaining exist visas for British subjects wishing to leave the province.

- 104. Negotiations were carried on during the year between the Government of India and the Chinese Consulate-General at Calcutta with a view to reaching an agreement whereby the gold recovered from Ma Hu-shan and his Tungan followers should be handed over to the consul-general, after deduction of a sum to cover the cost of repatriation to Hong Kong and thence to China of eighty-four destitute Tungan refugees, together with a sum sufficient to cover the claims for compensation by British Indian subjects in Sinkiang who suffered losses as the result of looting during the Tungan rebellion.
- 105. Correspondence also took place between His Majesty's Consul-General at Kashgar and the Sinkiang Government regarding the Darwaza district on the Indian frontier. The Provincial authorities claim the whole of this area as Chinese territory, while the Government of India point out that the Mir of Hunza has long established rights over the district.
- 106. In accordance with instructions received from the Government of India, His Majesty's Consul-General at Kashgar assumed charge of Swedish interests in Sinkiang on the 9th March, 1938. Swedish missionaries had maintained four mission stations in the province. Only two of these were occupied at the beginning of the year, at Yarkand and Kashgar. In February the missionaries at Yarkand were compelled, owing to a boycott organised by the Provincial Government, to leave for Kashgar, and all mission work having thus been brought to a standstill, the mission authorities decided to send all their people home. They left, accordingly, in June with the assistance of His Majesty's Consul-General. Three men who had remained in Kashgar also left in August, having received a hint from the Administrative Commissioner that their presence was no longer desired.
- 107. Major K. C. Packman, His Majesty's Consul-General, departed for India from Kashgar on the 2nd July, leaving His Majesty's Consulate-General in charge of Mr. M. C. Gillett as Acting Consul-General until the arrival on the 18th October of his successor, Major H. H. Johnson, C.I.E., M.M.
- 108. Early in the year the provincial authorities, through the Central Government, refused to grant permission for the relief of the consulate guard, on the ground that conditions in Kashgar were normal and no guard was necessary. The present Hunza guard accordingly stayed on in Kashgar for an extra year.

(f) Tibet.

- The removal of the Chinese Government towards the west has directed attention towards the instability of the borderlands of Sikang, and has led to considerable activity in that part of the world. The Chinese desire to bring Tibet under the Chinese flag still persists, and General Liu Wen-hui, the war lord of Sikang, has devoted considerable energy to this end. There are indications, however, that the Central Government would prefer to achieve their ends without his aid. They attempted to strengthen their hold over Sikang by decreeing in July the transfer of fourteen hsien districts from Szechuan to Sikang, and arranging for financial assistance from Szechuan to make Sikang economically self-supporting, and also by elevating Sikang to the status of a province, under General Liu Wen-hui, as chairman, with effect from the 1st January, 1939. Other indications of a forward Chinese policy towards Tibet were the establishment, with Central Government assistance, of a strong Kuomintang headquarters at Tachienlu and the inauguration by the Central Government of an educational movement among the lamas at that place. Great efforts have also been made to complete a motor road between Tachienlu and Yachow.
- 110. Of significance also were the elaborate arrangements made by the Central Government in connexion with the journey of Mr. Tai Chi-tao, the president of the Examination Yuan, to Kanze to take part in the funeral rites of the Panchan or Tashi Lama, who had died there on his way back to Tibet in November 1937. Mr. Tai Chi-tao is reported to have distributed largesse

with a generous hand, and it has become clear that the Chinese Government are using the Tashi Lama's body as a pawn in their political game, and will not permit its removal to Lhassa except on their own terms.

111. In Lhassa the Chinese mission continued to make capital out of the disturbed conditions arising out of the incompetent Government of the regency and the intrigues accompanying the recognition of a new Dalai Lama. Earlier in the year it was rumoured that the Tibetans were welcoming the Japanese advance in China as a possible check on the unwelcome attentions of the Chinese. The latest reports from Lhassa state, however, that the Japanese are regarded as a worse menace.

112. Partly to counteract the Chinese mission's activities, and partly in order to keep a watch on possible Japanese designs on Tibet, the Government of India agreed in September to the continuance of the British mission in Lhassa for a further year.

III.—FOREIGN RELATIONS.

(a) Japan and Attempts at Mediation.

- 113. At the end of 1937, as recorded in last year's report (paragraph 66), the Japanese Government had communicated to the Chinese Government, through the medium of the German Ambassador, their "basic conditions for peace." These were rejected by the Chinese, but the German Ambassador was asked in the early days of January to try to obtain from the Japanese Government an elucidation of their terms in greater detail. On the 18th January the Japanese reply was communicated to the Chinese Government. It was to the effect that the Chinese Government had that the Japanese proposals before them for some time, and the Japanese Government could only regard the request for elucidation of their terms as indicating a lack of sincerity and a desire to elude negotiations. The Japanese Government had therefore no option but to bring negotiations to an end.
- a statement of their policy towards China declaring that they would cease to negotiate with the Chinese Central Government and that they looked forward to "the establishment of a new régime" with which they could co-operate for the adjustment of relations and for the building up of a rejuvenated China. The breach was made complete by the departure of the Chinese Ambassador from Japan on the 20th January and of the Japanese Ambassador from Shanghai on the 28th. The Japanese Embassy in China remained in the hands of a chargé d'affaires until the 6th March, when Mr. Masayuki Tani was appointed with the rank of minister "to take charge of the Japanese Government's diplomatic affairs in China." Mr. Tani remained at his post, wielding no influence over his own military and naval authorities, and clearly conscious of the anomaly of his position—he was not accredited to any Government—until the 18th December, when he departed for Japan, leaving his embassy again in charge of a counsellor.
- In February and March the Italian Ambassador made a series of approaches, apparently on his own responsibility, to Mr. T. V. Soong in Hong Kong. These appeared to be primarily designed to undermine the position of General Chiang Kai-shek, but failed in their object. In June the Italian Ambassador tried again, this time sending an emissary to Mr. Wang Ching-wei, suggesting that all that was needed to set negotiations going was a personal letter from Mr. Wang to the Japanese Prime Minister to the effect that henceforth the policy of the Chinese Government would not be anti-Japanese. It was explained to Mr. Wang that the Japanese Government were still reluctant to have any direct dealings with General Chiang Kai-shek, but that they were now not unwilling that he should remain in the background. Mr. Wang Ching-wei apparently refused to enter into negotiations on his own behalf and nothing further came of the proposals.
- 116. Suggestions that His Majesty's Government in the United Kingdom should offer to mediate, possibly in concert with the United States Government, were thrown out on several occasions during the first half of the year by the

Japanese Ambassador in London. Inasmuch as it was not clear whether these suggestions had the backing of the Japanese Government and since, in any case, it was apparent that an essential condition on the Japanese side was the elimination of Chiang Kai-shek, His Majesty's Government took no initiative. Chinese morale was high, and there was no prospect of finding terms acceptable to both sides.

- When in Hankow in April, His Majesty's Ambassador had understood from Chiang Kai-shek that an essential condition of Chinese agreement to negotiations was the withdrawal of Japanese troops from all provinces in North China other than the three originally composing Manchuria. In July His Majesty's Ambassador again gained the impression that, although determination to continue resistance was now no longer coloured by the optimism of a few months before and there was much talk of peace negotiations, any solution which involved the withdrawal of Chiang Kai-shek was out of the question. Hankow, however, His Majesty's Ambassador was asked by the Chinese Minister for Foreign Affairs whether His Majesty's Government would be willing, in concert with the United States and French Governments, to address simultaneously to the Chinese and Japanese Governments notes offering the good offices of the three Powers to bring about a peaceful settlement of the hostilities. démarche was made a few days later by the Chinese Ambassador in London. After discussion of this proposal between the three Powers concerned, it was agreed that there was no possibility whatever of finding terms which would be acceptable to both sides, and that in these circumstances it would be undesirable to make any approach to the Japanese Government.
- 118. In October His Majesty's Ambassador at Tokyo received a suggestion from his German colleague that as soon as Hankow had fallen Germany should use her influence on Japan to propose reasonable peace terms, and that in her turn Great Britain should use her influence on Chiang Kai-shek to accept them. Tentative discussion of possible terms with the Japanese Government, however, led to the conclusion that the time had not come when successful negotiations could be undertaken.
- 119. The question of mediation remained in abeyance until December, when it was brought into the foreground by Mr. Wang Ching-wei's response to Prince Konoye's overtures. As described in paragraph 65 of this report the Chinese Government successfully frustrated this attempt to meet the Japanese half-way, and the year ended with a reaffirmation of their determination to continue resistance.

(b) League of Nations.

- 120. On the 2nd February the Council adopted a resolution calling the most serious attention of the members of the League to the terms of the resolution passed by the Assembly on the 6th October, 1937, expressing moral support for China in her conflict with Japan and recommending that members of the League should refrain from taking any action which might have the effect of weakening China's powers of resistance and should also consider how far they could individually extend aid to China.
- 121. At its next meeting, on the 14th May, the Council passed a further resolution calling upon members of the League to take into serious and sympathetic consideration requests they might receive from the Chinese Government in conformity with previous resolutions and expressing sympathy with China in her struggle against Japanese invasion.
- 122. In September the Chinese Government appealed to the Assembly of the League to invite Japan to accept the obligations defined in article 17 of the Covenant (by which a non-member State involved in a dispute might be asked to accept membership of the League for the purpose of that particular issue). Japan rejected this invitation on the 22nd September, and on the 30th the Council adopted a report declaring that, in view of Japan's refusal, the provisions of article 16 of the Covenant were applicable, and that members of the League were entitled not only to act as before on the basis of the Assembly's finding that the Japanese attack on China was unjustified, but also to adopt the individual

measures provided in article 16. The report went on to recall the previous resolutions of the Assembly and the Council, calling upon members of the League to consider what action they could take individually to assist China and to state that, while co-ordination of the measures that had been or might be taken by the Governments concerned could not yet be considered, China had a right to the sympathy and aid of the members of the League who should not forget their obligations under the earlier resolutions.

- 123. The only immediate effect of this resolution was the decision of the Japanese Government on the 3rd November to cease henceforth to co-operate with the cultural and technical organisations of the League.
- 124. At a meeting of the Opium Advisory Committee at Geneva on the 23rd June, resolutions were adopted drawing the attention of the League Council to the seriousness of the narcotic situation in the Far East and to charges of Japanese participation in the drug traffic which had been made by the United States and Chinese delegates.
- 125. The Chinese delegates on several occasions during the year called the attention of the League to the methods of warfare used by Japan in China, with particular reference to the air bombing of open towns and to the use of gas. At its meeting on the 30th September the Council adopted a resolution asking Governments of States represented on the Council and on the Far East Advisory Committee having representatives in China to investigate through the diplomatic channel alleged cases of the use of poison gas by the Japanese forces.
- 126. The United Kingdom representative at this meeting said that he must observe that evidence with regard to the use of gas by the Japanese was conflicting and that he could only accept with reserve the Chinese representative's statements on this subject.
- 127. On the 17th September the President of the Council presented a report based on the report of the Council's Committee for technical collaboration with China, calling upon the Council to recommend to the Assembly the provision of the necessary credits for the continuance of the work of the anti-epidemic commission in China and of normal technical collaboration between the League and China.

(c) British Commonwealth.

His Majesty's Embassy.

128. The headquarters of the embassy throughout the year have been at Shanghai, where the former offices of the commercial counsellor and financial adviser have been expanded to accommodate a full embassy staff. From the point of view of contact with the Chinese Shanghai has obvious and serious disadvantages, but an embassy there can at least keep in touch with consulates all over China, with the British business community, with most other foreign missions and with the outside world. For the purposes of liaison with the Central Government a diplomatic mission consisting of a senior member of the diplomatic staff and for the greater part of the year the assistant military attaché, has been maintained at the capital. Until October, when the fall of Wuhan became imminent, the mission remained at Hankow. It has since been established at Chungking, having moved up-river by gunboat. The embassy at Peking has remained open throughout the year. It was in charge of a diplomatic secretary until the beginning of November, when His Majesty's Consul at Peking assumed charge with the local rank of first secretary.

129. Sir Archibald Clark Kerr, K.C.M.G., arrived at Shanghai in February to take up the post of His Majesty's Ambassador to China. At the end of March he travelled by way of Hong Kong, Canton and Hankow to Chungking, where he presented his letter of credence to the chairman of the National Government of the Republic of China on the 12th April. At the end of June he made another journey via Hong Kong to Hankow, where he stayed from the 2nd to the 25th July to maintain direct contact with the officials of the Central Government. On his return to Shanghai he travelled via Changsha and Kweilin (in Kwangsi Province), which he was the first foreign ambassador to visit, to Wuchow on the West River, whence he returned by gunboat to Hong Kong. He left Shanghai

for the third time on the 18th October. By the time he reached Hong Kong the Japanese advance on Canton and Hankow had made a journey up the Canton—Hankow Railway out of the question, so he travelled by destroyer to Haiphong in Indo-China and thence by rail to Kunming in Yunnan. He left Kunming by car on the 29th October bound for Kweiyang and Changsha, where he met General Chiang Kai-shek, before returning by car to Chungking. He spent four days in the capital meeting ministers and officials and flew back to Hong Kong on the 19th November.

130. Other members of the embassy staff, notably the military and air attachés and the commercial counsellor also did a considerable amount of travelling during the year.

British Policy.

- 131. The governing factor in Anglo-Chinese relations throughout the year has been the undertaking given by His Majesty's Government in the United Kingdom in common with other Governments, at Geneva in 1937 and renewed in 1938, that they would consider how far they could individually extend aid to China in resisting Japanese aggression. The League Assembly's resolution of the 6th October, 1937, the Council's endorsement of that resolution on the 2nd February, 1938, and the various statements made with reference thereto by His Majesty's Government in the United Kingdom aroused extravagant but not unnatural hopes in China that His Majesty's Government would shortly come to her assistance with practical measures of support. Direct military aid has never been expected, and responsible Chinese leaders have, on the whole, shown an appreciation of Great Britain's difficulties nearer home, which have made the fulfilment of her undertakings by no means an easy task. The Chinese have, however, never ceased throughout the year to remind His Majesty's Ambassador of these undertakings and to ask what means were contemplated for carrying them into effect.
- 132. As early as January Dr. H. H. Kung asked whether it would be possible for His Majesty's Government to give China a loan for the support of the Chinese currency and the service of Chinese loans. He hinted that a similar loan had been arranged in the United States. This latter statement proved, however, to be premature and to have been designed by Dr. Kung primarily as a means of strengthening his own political position; no response was made to his suggestions.
- 133. On the arrival of His Majesty's Ambassador in China in February, Mr. T. V. Soong produced a rather more concrete proposal for a loan of £20 million, to run for fifteen years and secured on the proceeds of the Chinese monopoly of wolfram and antimony production, with surplus customs revenues as collateral security. The purpose of the loan was to be currency stabilisation rather than the purchase of munitions. This proposal had the support of His Majesty's Ambassador, who urged in May that there was force in General Chiang Kai-shek's claim that to some extent the Chinese were fighting Great Britain's battle in the Far East as well as their own, and that with British support the Chinese themselves might well be able in time to bring about a situation in which the Japanese would be obliged to assent to peace terms under which a measure of protection to British interests would be secured.
- 134. Examination of Mr. Soong's proposal in London made it clear that, for reasons of political expediency, a direct loan by His Majesty's Government was out of the question, and although various attempts were made to interest British commercial groups in the Chinese proposal, it became apparent that the security offered was not sufficient and that nothing could be done on this basis without a very large Government guarantee. The Chinese Government were informed that, while His Majesty's Government would be ready to consider any practical proposals for affording assistance to China, it was not expected that they would be able to provide this guarantee.
- 135. His Majesty's Government were, however, interested in proposals designed to give British interests control of China's production of wolfram and antimony, and the proposal for a loan with political backing was considered by

the Cabinet in July. It was decided, however, that in present circumstances the risks involved in any such direct political loan by His Majesty's Government were too great to permit of its being given.

- 136. This decision caused acute disappointment in China, and hints began to be thrown out that China would have to consider the reorientation of her foreign policy and that the direction this would take must depend upon the policy of Great Britain. During his visit to Hankow in July His Majesty's Ambassador was urged that British policy should be made clear without delay.
- 137. His Majesty's Government meanwhile continued their consideration of alternative means of assisting China. These included the improvement of communications by road, rail and air, between Burma and Yunnan, and also the provision, through the Export Credits Guarantee Department, of credits to finance the purchase by China of essential supplies, such as lorries, telegraph equipment and railway material.
- 138. When His Majesty's Ambassador visited him in Changsha in November, Chiang Kai-shek renewed the previous requests for a definition of British policy in the Sino-Japanese dispute, and for an early decision upon the question of assistance. Chiang Kai-shek contended that tacit acquiescence by Great Britain in the Japanese occupation of South China would spell a blow to British prestige and to the British position in the Far East, which might well prove irretrievable. He made an earnest appeal for British financial assistance for the support of Chinese currency, adding that this was a final appeal and that Great Britain and China were at the parting of the ways. He alluded to the recent British loan to Czecho-Slovakia as having made a painful impression in China, and urged that China's case was no less deserving. He also declared that if help were not forthcoming he would have to look elsewhere for friends. He instanced Soviet Russia, but said also that he believed he could come to terms with Japan on condition that China joined with her in excluding Great Britain from the Far East. In reporting this interview, His Majesty's Ambassador emphasised that China's determination to continue resistance was unshaken by the Japanese occupation of Canton and Hankow, and urged the importance of retaining China's goodwill as an essential guarantee of Great Britain's future in the Far East. He expressed the opinion that the time had come for a final decision whether His Majesty's Government were to render immediate practical assistance to China or to withdraw from their Geneva undertakings and pin their faith on the assurances of Japan, and he urged that the whole question of financial assistance to China be re-examined.
- 139. After his subsequent visit to Chungking His Majesty's Ambassador reported that in talks with him Mr. Wang Ching-wei, Dr. H. H. Kung and Dr. Wang Chung-hui had gone over much the same ground as General Chiang Kai-shek. As put forward by the Minister for Foreign Affairs the Chinese Government's requests were, first and foremost, that His Majesty's Government should give them financial help, and, secondly, that His Majesty's Government should without delay and in a public and striking way take a stand on the Nine-Power Treaty and put into early effect reprisals against Japan.
- 140. As regards financial assistance, His Majesty's Government were already giving consideration to a proposal made to His Majesty's Ambassador by T. V. Soong in October that the British and the Chinese banks respectively should each contribute £3 million towards the establishment of a Chinese currency stabilisation fund, and towards the end of December they suggested at Washington that if similar assistance were forthcoming from the United States banks the scheme's prospects of success would be greatly improved. His Majesty's Government also introduced legislation in Parliament towards the end of the year, empowering the Board of Trade to give guarantees in respect of imports from the United Kingdom up to £10 million. It was intended that, in granting these guarantees, political considerations should be taken into account, the transactions not being judged on a purely commercial basis as is the practice of the Export Credits Guarantee Department, and that, subject to agreement on detailed terms, guarantees up to £500,000 would be given for lorries for the Burma road.

- 141. Efforts have also been made on the Chinese side to establish an organisation in London which will handle the sale of Chinese products in the United Kingdom and other free exchange countries, and make the proceeds available for purchases of goods in the United Kingdom to provide the basis for guarantees by the Export Credits Guarantee Department. These efforts, if successful, should greatly assist in overcoming one of the principal difficulties of giving assistance to China, which has been the lack of precision in the proposals put forward on the Chinese side and the lack of effective machinery for carrying them out.
- 142. Another difficulty has been the attitude of the United States. The crisis over Czecho-Slovakia in September made it clear that His Majesty's Government, owing to their preoccupations in Europe, were in no position to take a strong line in the Far East without the full support of the United States Government. The latter, as always, have been obliged to move slowly and to keep in step with public opinion. Towards the end of the year there were signs that public opinion in the United States was steadily becoming aware of the menace to the United States constituted by the "new order in East Asia" which was now being proclaimed by Japanese leaders as their country's goal in the China war. The United States Government have consequently been able to take a firmer line.
- as to make possible a joint policy of reprisals against Japanese attacks on third-Power interests in China, to be carried out concurrently with the policy of assistance to China. The question of bringing pressure to bear on Japan has been under consideration by His Majesty's Government for some months, and at the end of August His Majesty's Ambassador was asked to furnish suggestions, based on the experience of Japanese methods in China, regarding the retaliatory measures which might be introduced in British territory against, for instance, Japanese shipping and banking. In forwarding his proposals, His Majesty's Ambassador expressed the opinion that a policy of pin-pricks, which would exasperate without seriously injuring Japan, was to be avoided, and that a gesture, such as the denouncing of the Anglo-Japanese Commercial Treaty of 1911 would be far more effective, not only in giving pause to Japan, but also in providing that practical encouragement and indication of Great Britain's attitude for which the Chinese have long been hoping.

Incidents.

- 144. The questions of high policy dealt with above are related to factors outside the purview of this embassy, such as the situation in Europe, the attitude of the United States and the progress of British rearmament. The day-to-day work of the embassy, and of the consulates in occupied China, has been rather concerned with watching the effect on British established interests, of the Japanese invasion of China, and in endeavouring to secure redress for numerous incidents arising out of the action of the Japanese armed forces. The impact of the hostilities on British interests is described in a subsequent section of this report. Here mention may be made of the more important disputes in which British subjects were involved.
- 145. As a general rule attempts have always been made to settle such incidents locally in the first instance. Such attempts have been rendered difficult by the Japanese genius for evading responsibility and by the lack of authority, vis-à-vis their military and naval authorities of Japanese Consuls, who are nevertheless often the only means of contact with foreigners. The expedient of representations to the Japanese Embassies in Shanghai and Peking was also tried but abandoned when it became clear that it merely delayed rather than hastened a settlement. Satisfaction of a sort was generally obtained eventually, but only after long delay and, in most cases, after the matter had been taken up in Tokyo.
- 146. At the beginning of the year the Japanese troops were still badly out of hand, and indignation spread throughout the world as information gradually became available about the excesses which had accompanied the occupation of Nanking, Wuhu, Soochow and Hangchow, and innumerable small towns

and villages up and down the country. At the end of January General Homma was sent to Shanghai and Nanking to restore discipline and a gradual improvement followed. The effects of the indiscipline were felt, however, in two cases of assault against British sergeants in the Shanghai Municipal Police, which occurred about the New Year. In Peking British military officers were twice, in January and again in April, assaulted by Japanese soldiers at the Peking railway station, while in Tientsin trouble arose in January out of threats by the Japanese gendarmerie to enter the British Concession and forcibly to remove a Chinese accused of anti-Japanese activities.

147. In Shanghai the effects of efforts to restore discipline were not reflected in any improvement in the relations between the British and Japanese military forces, and in March, April and May numerous cases occurred in which British troops and officers were threatened and insulted, and attempts made to interfere with British military transport arrangements. The anti-British feeling among the Japanese troops was such that the mere suspicion that a person was British was often enough to lead to interference by Japanese sentries. A particularly bad case occurred in May when a well-known British resident of Shanghai was arrested by Japanese soldiers while on a walk, detained for eleven hours, submitted to close questioning, which failed, however, to reveal any reasonable grounds for his detention, and when his British nationality became known brutally beaten. The position improved again after a visit paid to Shanghai at the beginning of June by the military attaché to His Majesty's Embassy at Tokyo, and it gradually became clear that the Japanese Government were making a serious effort to enforce discipline.

Isolated incidents, however, continued to occur. In particular Japanese airmen were at fault, and several flagrant instances of the bombing of clearly marked British mission and other properties in the interior came to notice between July and November. Fortunately none of the attacks was as serious in its consequences as those made on Sir Hughe Knatchbull-Hugessen or on shipping on the Lower Yangtze last year; but one which might have had disastrous repercussions occurred on the 24th October. Six Japanese heavy bombers flying at about 3,000 feet dropped a large number of bombs around the British gunboat H.M.S. Sandpiper while she was at anchor off Changsha, causing damage to her superstructure but, fortunately, no casualties. Japanese sought to argue that the airmen were bombing a concentration of Chinese junks alleged to be carrying troops and had not seen the Sandpiner. Inasmuch as the Japanese knew that a British gunboat was always stationed at Changsha, the Sandpiper was carrying special identification marks on her awning and superstructure, and the visibility was good the Japanese arguments were found inacceptable. The matter was finally regarded as settled on the basis of a letter addressed to the British Commander-in-chief by the Japanese Commander-in-chief expressing his sincere regrets for the damage caused and undertaking on behalf of the Japanese Government to defray the cost of the necessary repairs.

Claims.

149. An office has been established in His Majesty's Consulate-General at Shanghai for the preparation of claims for compensation against the Japanese or Chinese Governments in respect of damage sustained by British subjects as a result of the hostilities. General instructions regarding the preparation of such claims were sent early in the year to all consular officers in China. By the end of the year claims to the total value of roughly £235,000 had been sent to Tokyo for presentation to the Japanese Government, and of about £107,000 to the diplomatic mission for filing with the Chinese Government. Many more claims still remained to be assessed and presented. No payment had been received from either Government by the end of the year in respect of compensation for the losses suffered by British civilians. The only claims which had been paid were those addressed to the Japanese Government in respect of injuries caused to British sailors and soldiers at Wuhu and Shanghai in 1937, and in respect of damage to H.M.S. Ladybird in the incident at Wuhu on the 12th December, 1937. Compensation was also secured locally from the Japanese authorities in respect of cars removed from the British Embassy compound in Nanking after the Japanese occupation of the capital

150. A memorandum handed to the Japanese Vice-Minister for Foreign Affairs by His Majesty's Ambassador at Tokyo on the 24th December, 1938, contained a list of no less than sixty cases in which the Japanese Government had failed to give any satisfaction in reply to representations made by His Majesty's Embassy on the subject of the treatment by the Japanese authorities of British rights and interests in China. Cases which had been satisfactorily settled numbered only ten.

Relief.

- 151. The British Fund for Relief in China have continued to do all in their power to relieve civilian distress, which with the unprecedented migrations which the war has caused (some estimates claim that 180 million people have been forced to leave their homes) has reached tragic proportions. The funds and supplies available barely touch the fringe of an immense problem, but they have been distributed as impartially as possible where the need has seemed greatest.
- 152. His Majesty's Ambassador has also lent his support to appeals from the International Red Cross and the Red Cross Society of China for assistance and supplies for the treatment of wounded Chinese soldiers. Here again, however, the problem is so vast, the inefficiency and lack of equipment of the Chinese army medical service so notorious, and Chinese losses in consequence so heavy that nothing short of complete reorganisation is likely to be effective.

Weihaiwei.

- 153. The Weihaiwei Rendition Agreement of 1930 assured certain facilities to the Royal Navy, who use the port and island of Liukungtao as a summer base. The facilities will be due for renewal in 1940 and after consultation with the Commander-in-chief, His Majesty's Ambassador has recommended that the Chinese Government be requested without delay to agree to their extension on the existing terms for a further period of ten years.
- 154. Meanwhile, letters were exchanged with the Chinese Government on the 31st December providing for the renewal for a further year of the special facilities for drill and rifle practice on the Island of Liukungtao, which the Royal Navy have hitherto enjoyed under Article 3 (3) of the Rendition Agreement. Hitherto the necessary annual permission has been applied for and granted in letters exchanged at Weihaiwei between His Majesty's Consul and the local High Commissioner. Since the latter post is now held by a puppet official the only appropriate means of renewing the permission for 1939 was an exchange of letters with the Waichiaopu at Chungking.

Hong Kong.

- 155. The mere existence of Hong Kong was of inestimable value to China in the prosecution of the war. But for the fear of complications with the British colony the Japanese would probably have attacked Canton long before October, and meanwhile Hong Kong was not only China's principal channel for the import of war supplies but a valuable base for the establishment of Government trading organisations to maintain commercial contact with the outside world. Considerable numbers of Chinese officials and business men settled in the colony, and there was continual coming and going between Hong Kong and the interior of China, which was facilitated by the special temporary arrangements made to permit of the landing in the colony of planes of the Eurasia Aviation Corporation operating a regular service with Hankow.
- 156. Despite persistent Japanese allegations to the contrary the neutrality of Hong Kong was strictly preserved. Early in the year draft emergency regulations were prepared for issue, should the occasion arise, to assist the Government in this task. On the 17th February three Chinese war vessels which had remained in Hong Kong territorial waters were interned and kept in the colony for the rest of the year. Efforts such as these did not, however, prevent the occurrence of incidents, and on three occasions representations have had to be made against the violation of Hong Kong territorial waters by Japanese armed vessels, while there have been numerous cases of unprovoked attacks on Hong Kong fishing junks outside territorial waters, no less than seventy-one attacks being recorded during the second half of 1938.

157. During the first nine months of the year, trade boomed in the colony, but with the fall of Canton in October and the complete cutting of communications between Hong Kong and the Chinese mainland the position was entirely changed. The Japanese have disclaimed any intention of blockading the colony, but the position during the last three months of the year made it apparent that they had it in their power to do considerable damage to the colony's interests should they so desire.

158. During the operations around Canton the Japanese were at pains to avoid complications with Hong Kong, although in the course of subsequent mopping up operations near the colony's border frontier incidents occurred which had to be taken up immediately at Tokyo. During these operations about a thousand Chinese troops crossed the border into the colony and were disarmed

and interned.

159. The influx of refugees proved a serious problem to the colony throughout the year. At the end of May the Governor circularised certain consuls in South China, warning them that housing accommodation in Hong Kong had reached saturation point. In fact during the first five months of 1938 those entering the colony exceeded those leaving by 63,000. The situation was further aggravated by the Japanese military operations later in the year and the colony's resources being already taxed to the utmost arrangements were made by the Emergency Refugee Council to establish three refugee camps at points on the Chinese side of the border. At the end of the year the excess population in the Island of Victoria and in Kowloon was estimated at three-quarters of a million and half a million respectively.

160. The question of the renewal of the lease of the Kowloon new territories, which terminates in 1998, was given consideration during the year, the Governor urging that, from the point of view of commercial interests in the colony, the time had come for the matter to be settled and that present conditions presented an opportunity for securing renewal which might not recur. In supporting the Governor's recommendations His Majesty's Ambassador suggested that the renewal of the lease might be considered in conjunction with the grant of financial assistance to China. On consideration of the matter in London, however, it was decided not to proceed with the proposal. It was felt that not sufficient data was available for calculating the commercial importance of Hong Kong to British trade and for estimating the present value of an extension of the lease, while from the defence standpoint the present lease could be regarded as satisfactory for the time being.

Burma.

While the importance of the improvement of communications between Burma and South-West China had been realised by the Chinese authorities since an early stage in the hostilities, the question was given added urgency by the fall of Canton and the disruption of all lines of communication between South-West China and the outside world except the French railway through Indo-China. Consequently, at the end of October a mission, under Mr. T. L. Soong, was sent to Rangoon to discuss with the Government of Burma the possibilities of developing In response to requests put forward by the mission, the the Burma route. Government of Burma had already before the end of the year agreed to make certain concessions, such as the relaxation of port regulations and safety restrictions on the transport of explosives, reduced freights on Chinese Government stores and an increase in the customs drawback on re-exports from seven-eighths to fifteen-sixteenths. In making these concessions, the Government of Burma expressed the hope that the Chinese Government would be prepared to consider in the same helpful spirit proposals which the Government of Burma hoped to put forward for the fostering of trade between the two countries. A Chinese proposal for the formation of a joint Sino-British or purely Chinese company to navigate the Irrawaddy was on the other hand not favourably received in Burma.

162. After feverish work during the whole of the year, the new road linking Kunming with the rail head at Lashio in Burma was open to light traffic by the end of the year and in December the United States Ambassador completed the journey by car in twelve days. More work remained to be done before it could be considered an all-weather road capable of standing the heavy traffic

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which it would be called upon to bear if the Chinese Government's plans matured. On the Chinese side the work has been pushed through at extraordinary speed, chiefly by levies of forced labour. The gradients and general methods of construction are reported to be good, although the surfacing and embankments have not stood up to the last heavy rains and a number of bridges still need strengthening. On the Burma side the road which has been brought up to an all-weather standard is reported to be narrower than that on the Chinese side.

- 163. Plans have also been under discussion throughout the whole year for the construction of a railway between Burma and China. Early in January proposals were put forward by the Chinese for the joint construction of such a line, which it was assumed would for the greater part of its length follow the route through Talifu which had been surveyed as early as 1905–6. As usual, however, the Chinese proposals were lacking in precision and their estimates both as to cost and the time needed for construction appeared to be overoptimistic. A further difficulty arose during the year through the French Government's insistence that certain rights which they had secured in 1914 to construct a railway between Szechaun and Kunming, the easiest and most profitable section of the proposed line, were still intact. However, some progress had been made by the end of the year. In particular the Committee or Imperial Defence had decided that the strategic objections which had hitherto been put forward to the construction of the railway were no longer valid. The Government of Burma, however, had not yet finally committed themselves to assist in the construction of the line. Meanwhile, the British and Chinese Corporation, in collaboration with a French banking group and the China Development Finance Corporation, had begun to prepare preliminary plans for submission to the Governments concerned; no scheme concrete enough for consideration by the Export Credits Guarantee Department had as yet been put forward.
- 164. Negotiations for the establishment of an air service between Burma and Yunnan also continued throughout the year. The chief difficulty was the Chinese Government's refusal to give guarantees that a British air service would be allowed permission to fly on from Kunming to Hong Kong and Shanghai. After alternative Chinese proposals for the formation of a joint company had been put forward and rejected, the Chinese scruples were eventually overcome and at the end of the year preparations were being made for an exchange of notes whereby a Chinese company, to be approved by His Majesty's Government in the United Kingdom, was to be given permission to fly to Rangoon or Akyab in return for permission for Imperial Airways to fly to Kunming and eventually, when conditions permitted, to Shanghai and Hong Kong. The proposed formation of a Sino-British company for further development of the route was to be left over for discussion at a convenient opportunity after the cessation of hostilities.
- 165. His Majesty's Government in the United Kingdom informed the Chinese Government towards the end of the year that they considered that the question of the Burma-Yunnan frontier, which had been left in abeyance after the 1937 meetings would have to be settled before construction of any railway could be begun, since the alignment of the projected railway which appeared to be generally favoured was likely to pass very close to the disputed Hopang salient. No reply had been received from the Chinese Government by the end of the year to the request of His Majesty's Government that the matter be given urgent consideration.

(d) France.

- 166. Towards the middle of the year the French Government were approached by the Chinese with suggestions for the conclusion of a non-aggression pact, for the despatch of a French military mission to China and for closer collaboration between the two countries. The first two proposals were politely rejected, while, as regards collaboration, the Chinese were assured that no possibilities of financial assistance for railway construction and similar projects would be neglected.
- 167. France, like Great Britain, was made the object of repeated attacks in Japan during the year, as being one of China's principal supporters. In July anti-French agitation in the Japanese press became acute and the

assistance which France was alleged to be affording China was made the pretext for the threatened occupation of Hainan Island, which it was hinted could be used as a base for attacks on Indo-China-Yunnan Railway.

168. The French have already strenuously denied that munitions, other than those contracted for before the outbreak of hostilities, are; in fact, reaching China up this line. The Japanese, when challenged, have failed to produce evidence of concrete cases such as could be investigated. The railway has certainly been used to its full capacity so far as imports into China are concerned, but the goods carried have been principally petrol, motor lorries and piece-goods, rather than actual munitions. Owing to its narrow guage and steep gradients the capacity of the railway is in any case small. On the other hand, expedients have undoubtedly been found for getting small quantities of French war material into China, such as the landing of munitions up-river from Haiphong so as to avoid the customs and also their transhipment in junks from vessels inside French territorial waters near the Chinese frontier to Chinese territory. A number of "Dewoitine" fighter aircraft are known to have been brought up the railway and assembled in Kunming, while supplies from France have also passed through Hong Kong.

169. French economic interests in China centre principally in Yunnan, where the only foreign bank is French, as are also the principal foreign export firms. These interests are likely to become more important with the development of the south-western provinces and the building by the French of the railway between Langson in Indo-China and Nanning in Kwangsi, which was to have been completed by the end of the year and would eventually be linked to the recently completed Siang-kwei line from Hengyang on the Canton-Hankow Railway to Kweilin, the capital of Kwangsi.

In the rest of China France's interests centre primarily in her concessions. These have all been confronted with problems very similar to those of the British Concessions. Their position has, however, been stronger, in that they have far fewer hostages in the form of trading interests outside the concessions and also that the administration of the concessions is more directly under the control of the French Embassy as represented by the local consul. This was made clear, for instance, in Canton, where the bombing of the Chinese city caused the residents to look to the concessions for refuge. The French authorities were able to take a stronger line than the British in excluding refugees, because there were not in the French concession, as there were in the British, important trading interests with a voice in the administration of the concession to whose very existence the The position is presence and free movement of Chinese staffs was essential. similar in Tientsin, where Japanese attacks against the concessions appear to have been directed impartially againt the British and the French. The French Concession in Hankow, chiefly owing to its central position, has in particular roused the ire of the Japanese, who have enforced a virtual blockade since their occupation of Wuhan in October. In Hankow, as also in Shanghai, the French Concession has had to cope with a considerable increase in population. In Shanghai the French authorities, while working in collaboration with the settlement authorities, have as usual taken a determined and independent line and in particular the defence measures taken at the time of the European crisis in September called for strong protests from the local de facto authorities, which, so far as is known, remained unanswered.

171. The French Ambassador, M. Paul Émile Naggiar, made his head-quarters in the French Concession at Shanghai. He paid a visit to Hankow in April and left for Europe on transfer to Moscow on the 27th November, leaving his embassy in charge of a counsellor. His successor, M. Henri Cosmé, had not arrived in Shanghai by the end of the year.

(e) Germany.

172. The presence in China of the German military advisers, in contradiction of the Anti-Comintern Pact, continued to be a source of embarrassment to German official quarters. At the very beginning of the year it was being rumoured in Hankow that in view of the recent arrival of a large number of Soviet air advisers the Germans would not be allowed to remain much longer.

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It was not, however, until late in May that forty-nine of them received orders to return to Germany and not until July that they left Hankow. Although they were sorry to go and the Chinese naturally sorry to lose them, they had by that time completed their immediate task of preparing the defences of Hankow, and subsequent events would probably not have been materially affected had they stayed.

- 173. On the other hand, Sino-German relations have deteriorated since their departure. The German Ambassador left Hankow at the end of June and apparently no successor is to be appointed. The newly appointed Chinese Ambassador to Germany, Dr. Chen Chieh, was kept waiting in Berlin for many weeks towards the end of the year before being allowed to present his letter of credence to Herr Hitler. This caused general resentment in China.
- 174. German trade, which had made remarkable strides in China in recent years, has undoubtedly suffered as a result of the German Government's attitude and, although there have been frequent rumours that Japan was on the point of granting special privileges in China to her anti-Comintern friends, most available evidence goes to show that Germans are receiving no better treatment in occupied China than British subjects. Towards the end of the year it was learned that local negotiations had been proceeding at various ports in North China with a view to the conclusion of special trading arrangements on a barter basis between German merchants and various Japanese-controlled trading organisations.
- 175. Figures showing German supplies of munitions to China during the latter half of the year are difficult to obtain. During the first half she was undoubtedly one of China's principal suppliers: figures for the traffic through Hong Kong show that of the arms entering China by this route Germany supplied during the first six months of 1938 far more than any other single country.

(f) Italy.

- 176. Italy's interests in China are not important, and the anomaly of her position as a member of the Anti-Comintern Pact was not as apparent as Germany's. Italian supplies of munitions to China were not large, the principal contribution during the first seven months of the year being 101 armoured cars imported through Hong Kong. It was rumoured that Italy hoped to take advantage of Germany's reported undertaking to Japan that she would stop supplies in order to increase her own exports at Germany's expense.
- 177. Despite rumours to the contrary, no evidence was forthcoming of special privileges in China having been granted to Italy by Japan, although it was whispered that the handing back of the Italian Concession at Tientsin was under consideration.
- 178. Mention has been made elsewhere in this report of Signor Cora's somewhat shady attempts at mediation. On the 4th October he left Shanghai on transfer to a court post in Rome. His successor, Marchese F. M. Taliani di Marchio, arrived in Shanghai on the 18th October, but by the end of the year had not made any attempt to visit Chungking to present his credentials. His failure to do so has aroused indignant comment in the Chinese press, which has also reproached him with accepting the hospitality of the puppet mayor of Greater Shanghai.

(g) United States of America.

- 179. The United States Ambassador was at the seat of the Chinese Government, first at Hankow and since October in Chungking, during the whole of the year. In December he left Chungking for the United States, having been recalled for consultation with his Government. He travelled via Kunming and the new Yunnan–Burma motor road and proposed to fly to Europe from Rangoon.
- 180. United States missionary, educational and philanthropic enterprises are the most considerable in China and appear to have suffered more than those of any other Power as a result of the hostilities. On the 31st May the United States Ambassador at Tokyo addressed a note to the Japanese Government complaining of the continued occupation of United States property, including

the University of Shanghai, by the Japanese forces and the denial of access to missionary and other property in the Yangtze Valley. On the 19th October he wrote a further note enclosing a "partial list" of no less than twenty-nine instances of bombing of United States property in China by Japanese aircraft, all of which had occurred since the 1st May, 1938.

181. The American business communities in Shanghai and North China have shared the general indignation aroused by Japanese restrictions on trade and, during the last three months of the year, their Government appear to have decided that public opinion in the United States had developed sufficiently to allow them to make vigorous representations to the Japanese Government against these restrictions. The United States Ambassador's note of the 6th October on this subject was followed by that of the 7th November demanding the resumption of trading on the Yangtze and by the further representations which he made on the 31st December against recent Japanese pronouncements regarding the "new order in East Asia" and the "Japan-China-Manchukuo economic bloc."

182. The United States Government have afforded considerable assistance to China during the year by continuing the existing arrangements for the purchase of Chinese silver. In this connexion an interesting incident occurred in October when the *President Hoover*, the first Dollar liner to call at Shanghai since the hostilities began, was delayed at the instigation of the Japanese authorities when the latter learnt that she was to carry a consignment of bullion to the United States. The vessel sailed after twenty-four hours' delay without her cargo.

183. Another important measure taken by the United States Government towards the end of the year to assist China was the grant of a credit of U.S. \$25 million for financing exports to China, especially of "agricultural and manufactured products."

184. Finally, after the Union of Soviet Socialist Republics, the United States of America was the principal supplier of aircraft to China, fifty-one military machines having been imported from the United States through Hong Kong between the 1st January and the 31st July.

(h) Union of Soviet Socialist Republics.

a mystery throughout the year. Soviet union and China have been something of a mystery throughout the year. Soviet assistance has undoubtedly been considerable, although impossible to measure exactly. During the whole of the year the Chinese air force has been manned to a large extent by Soviet pilots and advised by Soviet experts. Moreover, China has been chiefly dependent on the Soviet Union for the supply of aircraft, and while the proportion of Soviet machines in the Chinese air force at the beginning of the year was 30 per cent., by the end of the year it had risen to 70 per cent. It should be remembered, however, that the effective strength never exceeded 300 service planes. The Soviet machines supplied were flown from the Union of Soviet Socialist Republics by way of Northern Sinkiang and Kansu. A considerable amount of Soviet war material also found its way to China through Hong Kong.

186. It is, however, easy to exaggerate the value and extent of Soviet assistance to China. Moreover, the presence of the Soviet advisers and airmen was not an unmixed blessing since they tended to be used for political ends. Notably during the month before the fall of Hankow General Chiang Kai-shek was acused of wishing to save his own troops, and in order to force him to accept the advice of the Chinese Communists the Soviet airmen refused to leave the ground for several weeks.

187. On the other hand, it cannot be suggested that relations between the Soviet Union and the Chinese Communists are by any means close. The latter are not Communists in any thorough-going Marxist interpretation of the word, and the Soviets are undoubtedly interested in them primarily as the backbone of the anti-Japanese movement in North-West China and as a buffer against Japanese aggressive designs. The Chinese Communists appear, however, to have received extremely little material support from the Soviet Union in their operations in the north-west.

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- 188. Shortly after the fall of Hankow three Soviet conseillers politiques arrived at the Chinese Communist headquarters in Shensi. Judged in the light of subsequent events their mission was probably the stiffening of Chinese resistance.
- 189. During the sessions of the People's Political Council held at Chungking at the beginning of November one of the three principal groups which emerged was a pro-Soviet group under the leadership of Mr. Sun Fo, the president of the Legislative Yuan. Mention has been made elsewhere in this report of the hints which began to be thrown out towards the end of the year that unless support were forthcoming from the democracies China might be obliged to seek Russia's friendship. There is no doubt that this prospect does not appeal to General Chiang Kai-shek.
- 190. Mr. Sun Fo visited Moscow in May and June. His visit was generally regarded as being concerned with the question of Soviet assistance to China.
- 191. The new Soviet Ambassador, M. Luganets-Orelski, presented his credentials at Chungking on the 23rd January. In his speech he declared that in the opinion of the Soviet Government "the existence and development of a united, truly independent, free China is one of the indispensable and most important bases of peace and friendship among the people of the whole world." He was recalled to Moscow from Hankow on the 17th June. Contrary to the expectation of the pessimists he eventually returned to China, and on the 21st October he established his embassy in Chungking.

IV.—BRITISH INTERESTS AND THE HOSTILITIES.

(a) Settlements and Concessions.

Shanghai.

- 192. The struggle between the endeavours of the Japanese to assert their predominance in Shanghai, and the international rights and interests in the settlement administration, as represented by the Shanghai Municipal Council, has proceeded throughout the year, and its end is not yet in sight.
- 193. The conflict has tended to centre round certain major issues—the Japanese demand for greater representation on the council and in the police force, their desire to obtain control of the Chinese law courts in the settlement, and to secure the withdrawal of the British troops from the Western perimeter; and, on the other side, the council's desire to re-establish municipal control in the Northern and Eastern Districts, and to discover some tolerable modus vivendi in the Western (Extra Settlement Roads) Area. In the course of negotiations, both in Shanghai and in Tokyo, the Japanese have sought from time to time to link up these various issues. The situation is further complicated, locally, by rivalries between various sections in the Japanese camp, each with its own axe to grind.
- 194. The year started with a full Japanese offensive, in the form of demands presented on the 4th January to the chairman of the council by the Japanese Consul-General accompanied by military and naval representatives. These demands, a pretext for which was found in a series of incidents arising out of the throwing of hand-grenades at Japanese soldiers by Chinese in the settlement, included the appointment of a Japanese co-secretary to the council, the strengthening of the Japanese element in the police force, and the placing of Japanese in controlling positions in all the important branches of the municipal administration.
- 195. After consultation with the British, American and French authorities, the council returned a considered reply to these demands on the 17th March. The reply, while sympathetic in tone, explained the inexpediency of making such drastic changes, but offered substantial concessions towards the increase and strengthening of the Japanese representation in the police force. This offer was accompanied by a request for the full restoration of council control in the areas north of the Soochow Creek. The Japanese Consul-General replied on

the 6th April, in a letter which was, on the whole, conciliatory in tone, but made no mention of the request for the restoration of council control in the Northern District.

196. Those questions, and others, such as the restrictions on access to British properties and removal of British cargoes from wharves in the Northern District, came under discussion in Tokyo, between His Majesty's Embassy and the Japanese Foreign Office. In the course of these discussions the latter intimated that the problem of the Western Extra-Settlement area might be solved by allowing the municipal council's police to take over the policing of that area if the British authorities would be willing, in return, to withdraw the British troops from the Western perimeter. It was felt, however, that the withdrawal of the troops could not be considered except as part of a general settlement which would have to include the restoration of council control over the Northern District.

- 197. The Japanese then (in September) offered to restore the Northern District to council control on certain conditions, which included their desiderata concerning police reorganisation and also the handing over of the law court (special district court) to the de facto (puppet) authorities. The terms were obviously inacceptable, but during the autumn the question of the Northern District came under discussion in Shanghai, between the council and the Japanese Consul-General. The negotiations, though slow, made definite progress, and by the end of the year an agreement was on the point of conclusion. The main points are that the Japanese will agree to the council reassuming police control, and promise to expedite the removal of various vexatious restrictions, and the council, on its side, will agree to measures for the increase of Japanese representation in the Shanghai Municipal Police, on lines essentially the same as those of the council's offer of the 17th March, 1938. This arrangement will mean a definite step forward in the reassertion of the council's rights, and will have been attained without the sacrifice of any important point of principle. It is to be noted that the Japanese demand for the handing over of the special district court, which was put forward in Tokyo, was not repeated in the subsequent discussions in Shanghai.
- 198. Meanwhile, a grave deterioration occurred in the conditions in the Western Extra-Settlement Area, where gambling and opium establishments sprang up in the enclaves, under Japanese protection, and in December the criminal elements who have resorted to those enclaves made their presence felt in a series of armed robberies on the extra-settlement roads policed by the council. No progress has been made towards finding a solution of the problem of the Western Extra-Settlement Area. In December the chairman of the council sounded the "puppet" mayor of the Greater Shanghai Municipality in order to see whether there was any possibility of his suggesting any way in which conditions in the enclaves could be improved. The "puppet" mayor's response had not been received at the end of the year.
- 199. To sum up, it may be said that during this anxious and difficult year the council have more than held their ground. The arrangement regarding the Northern District seems to be on the point of materialising, and represents a partial but definite advance towards the distant goal of normality. The question of the special district court has remained quiescent since the Japanese threatened to press it, at the beginning of the year, though it remains a latent cause of anxiety. The gains on the Japanese side were virtually confined to one empty symbol—the enforced hoisting of the five-barred flag adopted by the "Provisional Government" on the Shanghai customs-house (on Sundays and holidays only).
- 200. The Chinese Government also continued to take an interest in Shanghai questions, such as the fate of the special district court. This interest was manifested in particular at the time of the so-called "Lone Battalion" incident in August. These Chinese troops, who had been interned in the settlement, after their last stand in Chapei in November 1937, became restless and unruly, and in August repeated attempts to fly the Chinese flag in the internment camp finally necessitated intervention by the council's Russian regiment

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which guards the camp. Three of the Chinese died from injuries received in the *mêlée*. This occasioned much public indignation, but the matter was eventually settled by the council paying \$3,000 as a compassionate grant to the families of the three men.

Tientsin.

- 201. The position in Tientsin was clearer than that in Shanghai owing to the more specific rights enjoyed by Great Britain, France and Italy in their respective concessions. The concessions nevertheless proved a continual source of embarrassment to the Japanese; the more extreme elements regarded their mere existence as an affront and made little attempt to disguise their desire to get rid of them. The Japanese attacks were directed against both the British and French Concessions but the former bore the brunt.
- The principal Japanese complaints against the British Concession followed certain well defined lines. It was argued above all that the concession was being used as a base for the anti-Japanese activities of Chinese guerrillas, who were accused of using the protection afforded by the concession for keeping open radio communication with the Central Government and for planning their operations in the interior. Another grievance arose out of the fact that the Tientsin telephone exchange was in the British Concession and the Japanese desire that the local de facto authorities should be allowed to take over the Telephone Administration. The existence of Chinese banks in the British Concession was also alleged to be rendering impossible the Japanese plans for the introduction of a new currency in North China, since in view of the protection afforded by the concession foreign and Chinese merchants were able to finance their trade in Chinese Government currency. Some of the banks also held important silver reserves on which the Japanese, seeking a base for their new currency, cast envious eyes. Finally, they maintained that the concession was being used as a centre of anti-Japanese propaganda and intrigue, that newspapers were not subject to proper control (a ban was imposed on the circulation of the Peking and Tientsin Times in North China during the latter part of the year because of its alleged anti-Japanese tone), and that the books used and teaching given in the Chinese schools in the concession were anti-Japanese.
- 203. The situation only became acute during the latter half of the year, when pressure was brought to bear by the Japanese authorities to force Japanese residents and merchants to leave the British and French Concessions. At the same time the security of the British Concession and of British residents was menaced by the lawless conditions which the Japanese military had allowed to develop in the areas adjoining the concession. British businesses outside the concession also experienced difficulties and were for instance in some cases obliged to accede to demands that the Japanese gendarmerie must be allowed to enter their premises at any time and inspect their employees without permission.
- 204. In December a virtual blockade of the British and French Concessions was instituted, barricades being erected at all exits and passes demanded of all those wishing to go in or out. Movement of cargo was prevented, and there was occasional interference with the entrance of food supplies. The excuse given for these measures was the increase of Communist and anti-Japanese activities in and around Tientsin, but the real motive was undoubtedly a desire to isolate the concessions. It also seems likely that the new Japanese restrictions were, in part, an expression of their anxiety over the economic and military difficulties they were experiencing in North China and of their uncertainty as to what to do next.
- 205. Meanwhile, every effort was made to convince the Japanese authorities that genuine efforts had been made by the municipal authorities to preserve strict neutrality. In fact, answers were available to all the Japanese charges.
- 206. If the Japanese demanded that Chinese guerrillas be handed over to the *de facto* authorities, the Chinese Government were equally insistent throughout the year that this should on no account be done, and as a compromise it was decided that all such offenders should be interned in the concession until the establishment in Tientsin of a recognised Chinese administration to whom they could be handed over. As regards radio communication, regulations were issued by the municipal authorities making it illegal for any transmitting stations to be

operated without a licence, while all reasonable facilities were offered to the Japanese police for co-operation in the apprehending of offenders. The difficulty over the Telephone Administration was also solved by a compromise arrangement whereby the administration was first taken over, in the face of protests from the Chinese Government, by an inter-concession committee pending negotiations for its eventual transfer to the de facto authorities. Measures could obviously not be taken to compel the Chinese banks in the British Concession to use the Federal Reserve Bank notes, especially as this would have been directly contrary to the interests of British merchants, but towards the end of the year the British municipal authorities were obliged, partly in consequence of the refusal of Japanese ratepayers to pay in Chinese currency and partly because of the growing shortage of the latter, to accept the Federal Reserve Bank notes in payment of rates. Arrangements were made with the Japanese authorities for the sealing of the silver reserves so that there would be no possibility of their removal for the use of the Chinese Government. As regards anti-Japanese propaganda every possible effort was made by the concession authorities to prevent the printing and distribution of inflammatory pamphlets and literature and the books used in Chinese schools were carefully inspected.

207. The Japanese authorities, however, appeared to have deliberately wished to avoid discussion of specific measures such as these, and gave the impression that they preferred to believe any story of anti-Japanese activities which was brought to them, for instance by disgruntled ex-employees of the British municipal police with old scores to pay off, and to make use of such allegations to stir up ill-feeling against the concession in support of their boycott campaign. At the end of the year a virtual stale-mate appeared to have arisen. If the Japanese economic schemes were not going according to plan British traders on the other hand were suffering from the restrictions imposed upon them and it looked as though the situation were developing into a test of endurance.

Canton.

208. At Canton there had been no signs by the end of the year of any deliberate campaign on the part of the Japanese against the concessions on Shameen. The closure of the Pearl River which followed the capture of Canton and the interruption of all communications both with Hankow and with Hong Kong were in themselves enough to constitute a virtual blockade of British trading interests. In Canton itself, however, the Japanese authorities were at pains to establish friendly relations with the British Concession on their arrival and unnecessarily irksome restrictions appear to have been avoided. By the end of the year it had become clear that the Japanese had it in their power to bring severe pressure to bear on the concession should they so choose, but their desire to do so had not been made by any means so obvious as was the case in Tientsin.

Hankow.

- 209. In Hankow the position was more complicated, British rights in the Special Administrative District No. 3 being tenuous as compared with those enjoyed in Tientsin or Canton. The questions of safeguarding foreign property and of making some provision for the safety of the Chinese population in the event of a Japanese attack had been broached with the Japanese Government as early as December 1937, but the necessary undertakings of demilitarisation from the Chinese, which would bring the Japanese assurances of immunity into effect, were not forthcoming until the day before the Japanese arrived. Nevertheless foreign life and property were in general respected and the relatively few Chinese who had remained, although suffering violence, loss of property and eviction from their homes, were at least spared a repetition of the horrors which accompanied the occupation of Nanking.
- 210. Some months before a special force of about 100 British sailors had been sent to Hankow to reinforce the gunboat crews in case of trouble during the occupation. These men supported the Chinese police of S.A.D. 3 during the arrival of the Japanese, but were withdrawn after three days on the demand of the Japanese military authorities, who insisted on taking over the policing of the district themselves. At the meeting at which arrangements for the transfer were concluded it was made clear that the other administrative services were to remain



in the hands of the municipal bureau, of which a leading British resident had meanwhile been appointed chairman by the Chinese Ministry for Foreign Affairs under the Rendition Agreement of 1927, and that the arrangements were without prejudice to further discussion regarding British rights in the area. His Majesty's Consul-General informed the Japanese authorities officially that he considered the action of the Japanese military police in assuming the full duty of policing S.A.D. 3 was not in accordance with those rights. A similar reservation was made subsequently at Tokyo.

- 211. There had been little change in the position by the end of the year. Despite fears to the contrary, the British chairman of S.A.D. 3 remained in office, In practice, however, his powers were limited, and with Japanese police in control and the departure of practically all Chinese of any standing, the Municipal Bureau had no means of collecting rates to finance the continuance of such limited functions as it was permitted to fulfil. While the attitude of the Japanese has not been seriously hostile, there is no doubt that they aim at the eventual absorption of S.A.D. 3 into a larger administrative area and at the gradual elmination of the British share in its control.
- 212. The position of the British community is unhappy. While some of the more rigorous restrictions on their freedom of movement have been relaxed and some of the public services, such as the water supply, restored, the Japanese have made no secret of their intentions to keep the foreign community isolated and to obstruct the revival of their business. Indeed, so long as the Japanese are in military control of the Yangtze and refuse to permit British vessels to trade or British subjects to travel up-river, such British communities as have remained at occupied Yangtze ports are completely marooned. Besides those at Hankow, the foreigners at Kiukiang have remained ever since July isolated in a steamer to which they were obliged to retire at the time of the Japanese attack on the town, and, despite continued representations, have not been allowed to return to their property. Some thirty-six foreigners out of 180 at Kuling were evacuated with the assistance of the Japanese authorities in December. The rest, including about sixty British subjects, remain cut off in the hill station, which is in the occupation of Chinese irregular troops whom the Japanese have not troubled to clear out of the surrounding mountains. At Nanking there is a mere handful of British subjects who have secured special permission from the Japanese to return, but who can do no trading so long as the river remains closed.
- 213. Indeed, at the end of the year the position of all the British communities in the occupied ports—and these included practically all the important centres of foreign trade and residence—had become such that local remedies were no longer of any avail and the feeling was growing that their fate could only be decided by the adoption in London of effective measures of pressure against Japan.

(b) Trade and Investment.

Finance.

- 214. The hostilities between China and Japan have been described as a "war of currencies." Whilst this exaggerates the importance of the financial factor, it is of course true that the struggle turns to some extent on relative economic strength, and as hostilities continue the financial factor will be of increasing importance. During the past year Japan's attacks on China's revenues, through the occupation of her principal ports and railways and her attempts to undermine and displace the Chinese Government's currency in North China, have played an important part in supplementing her military and political campaign, and despite the misgivings of some Japanese bankers and merchants, they have been adopted by the Japanese army as essential to the fulfilment of their plans. Moreover, in view of the important foreign investments secured on Chinese revenues and of the interest of foreign merchants in the maintenance of a stable and convertible currency, the financial factor has been one of the principal causes of conflict between Japan and third Powers.
- 215. Japan's success in her attack on the Chinese Government's revenues may be gauged from the fact that, while no budget figures were published during the year, the loss of important trading centres and the general dislocation of commerce and transport was estimated to have cost the National Government over

three-fourths of its normal revenues (about \$1,000 million annually). The deficit was made up to some extent by "National Salvation Loans," totalling \$500 million, which are reported in the press to have been fully subscribed. The extent to which note issues have been increased is not known, but any increases appear to have been offset by hoarding, which has checked the tendency towards inflation. Strenuous efforts were made, as recorded elsewhere in this report, to supplement China's diminished revenues by securing aid from abroad, in the form of loans or credits from foreign countries. A Chinese mission despatched to the United States in October succeeded in arranging for a credit of United States \$25 million for the purchase by China of goods in the United States, and the possibility of similar assistance by His Majesty's Government was also under consideration. Chinese residents overseas also rendered valuable assistance to the Government, by direct purchases of war loans, and indirectly by remittances—estimated to total \$500 million—to their relatives in China. These remittances, in foreign currencies, were an important source of support for the exchange.

The effect of the fall in China's revenues has been felt by foreign holders of Chinese Government and railway bonds. Service of obligations secured on the Customs was rendered extremely difficult by the fact that, while total customs revenues for the year amounted to \$255 million (as against \$343 million in 1937), two-thirds of this came from ports under Japanese occupation, and none of the revenues so collected accrued to the Chinese Government. Nevertheless, with the exception of two loans, liability for which was denied by the Ministry of Finance, all loans secured on customs revenues were met in full by borrowing \$143 million from the Central Bank to make good for the lack of remittances from ports under Japanese control. The service of foreign loans cost \$78 million, and of internal loans \$129 million. Loans secured on railways did not fare so The Chinese Government denied responsibility for loan services where the whole of the line in question had passed from their control to that of the Japanese, and the latter asserted that, as a result of the Chinese Government's "scorched earth" policy, such heavy expenditure was incurred in repairing the lines and replacing rolling-stock that they could not accept responsibility for the loans. The Salt Administration was seriously disrupted by the hostilities, as the more important salt-producing areas fell into Japanese hands, and in September the Ministry of Finance announced its decision to defer amortisation on loans secured on salt revenues.

217. Japan's attempts to supplant the Chinese currency began in March, when the Japanese authorities set up a "Federal Reserve Bank" in Peking, with power to issue its own notes. One object of its establishment was to attack the Chinese currency by substituting the new notes for legal tender notes, and with the latter to buy foreign exchange. To prevent this the Chinese Government introduced restrictions on the sale by the Central Bank of foreign exchange at the official rate. An elaborate system was established whereby importers applied to the Central Bank for exchange, and weekly allotments at the official rate were granted after the applications had been scrutinised. The amount allotted gradually decreased, from half a million pounds weekly at first to only a few thousand later in the year, and the market became more and more dependent on the "open" or unofficial rate, which was supported by sales of export bills, and, in the autumn, by the Government banks selling sterling. In December the open market rate, which in January had with some difficulty been maintained at the official rate of 1s. $2\frac{1}{2}d$., was about $8\frac{1}{2}d$., and as export produce was still freely obtainable for legal tender notes, the rate would probably have been higher but for fears of Japanese attacks on the currency and of inflation by the Chinese Government.

218. Meanwhile the new currency issued by the "Federal Reserve Bank" made slow progress in North China. The sponsors claimed that by the end of the year over \$150 million had been issued, though the amount in active circulation was not believed to exceed \$40 million. This currency is nominally at par with the yen at 1s. 2d., but in fact is inconvertible into foreign exchange except by conversion first into Chinese legal tender, and thence into foreign exchange at the open market rate. The new currency is, however, accepted for conversion into yen, for payment of customs and other dues, and on the railways in North China. It has therefore some value in practice, and, aided by a shortage of legal tender notes, was at the end of the year in fairly general use in the areas directly

controlled by Japan in North China. On the other hand, in the countryside, even a few miles away from the railways and towns garrisoned by Japanese troops, the new currency was not merely useless, but even placed the holder in serious danger of reprisals from the local authorities.

219. In general it may be said that China has so far held her own in the "currency war." Despite the loss of three-fourths of its normal revenues, heavy purchases of war materials, an attack on the currency in North China, and general dislocation of transport and commerce, the Chinese Government, during the year, succeeded to a remarkable degree in retaining public confidence in legal tender notes and in avoiding widespread inflation.

Trade.

220. The figures for the foreign trade of China for the whole of 1938 are not yet available, but a comparison of the figures for the first eleven months of the year with those for the corresponding period of the previous year show that both imports and exports have fallen off.

	$(First\ eleven\ months)$				
		1937.	1938.		
Imports (in millions of St. \$)	 	903	821		
Exports	 	783	704		

- 221. It is remarkable that so much foreign trade should have been done in view of the general disruption of communications and the devastation caused by wars and floods.
- 222. The share of Japan in China's trade has increased from 16 to 22 per cent. for imports, and from 10 to 15 per cent. for exports, while that of Hong Kong in the export trade has risen from 18 to 33 per cent. The shares of most other countries have, however, fallen, Great Britain's from $11 \cdot 55$ to 8 per cent. for imports and from 9 to 7 per cent. for exports, the United States from 19 to 17 per cent. for imports and from 28 to 11 per cent. for exports, Germany's from 15 to $12 \cdot 7$ per cent. for imports and from $8 \cdot 6$ to 7 per cent. for exports.
- 223. The chief development during the last year has been the progressive imposition by the Japanese of various restrictions on trade in the occupied areas. The position has been most serious at Tsingtao, where the Japanese, unhampered by any foreign concessions, have, since last May, rendered the export trade more and more difficult. Permits to export have since then been required from the Japanese Naval Mission and these have in most cases been refused to British and other foreign firms. The mission is not prepared to give exact definition in writing of its requirements, but it has now made clear to foreign firms that all exports have to be financed through the Yokohama Specie Bank at a rate of 1s. 2d. to the dollar. After some negotiation, the mission has, however, allowed merchants to fulfil their existing commitments. The egg firms have, for instance, been permitted to fulfil their contracts for 1938 and some firms have been able to send goods to Shanghai for re-export abroad, or to South China.
- 224. By the end of the year, however, the trade of foreign merchants was at a standstill, and even the egg firms found that the Japanese proposed to stop their exports during the coming season. The aims of these restrictions were undoubtedly the need for supporting the new currency and for relieving the increasing difficulties of Japan's trading position. At the same time there was clearly considerable discrimination against foreign merchants. The large Japanese firms were exporting freely and were financing their exports themselves without selling their bills to the Japanese banks. Moreover, they were not doing so at the $1s\ 2d$ rate, but through Shanghai at the open market rate.
- 225. At Tientsin the foreign concessions prevented the Japanese from establishing the full control they had at Tsingtao, but nevertheless the free export of furs, skins, jute and hemp was forbidden in June, and of cotton in November. It is also almost impossible to obtain wool from Mongolia owing to the exchange and other restrictions imposed by the Meng-Chiang authorities. For a time last year, however, Tientsin enjoyed what almost amounted to a boom owing to the

large export of accumulated stocks, especially of cotton (mainly to Japan, though it was packed by British press-packers in Tientsin), and also to the fact that many Chinese were buying goods in preference to holding a currency the future of which was uncertain. This has now ceased, and the outlook for foreign merchants in Tientsin, as at Tsingtao, is gloomy, as it seems inevitable that the Japanese will introduce stricter measures of trade and exchange and control in order to compel the use of the new currency. The breakdown of communications between the railways and the guerrilla areas has restricted the flow of goods to and from the towns, and the present efforts of the Japanese to coerce the foreign concessions by a policy of encirclement into a more accommodating attitude towards their currency and other schemes, and to introduce tighter measures of trade control, will make things very difficult for the foreign merchant if they are successful.

226. Shanghai's trade is suffering from the continued closure of the Yangtze and the difficulties of communication with the consuming and producing areas of Central China. The total amount of trade done by the port was only just over half of that done in the year before. Here, too, the Japanese are attempting to control trade by the formation of companies to monopolise the purchase of raw materials such as silk and cotton, and by taking over Chinese concerns which were unable to move to areas not yet occupied by the Japanese armies.

227. The policy of the Japanese of forming companies to control every branch of trade or industry was illustrated by the inauguration in November of the North China Development Company and the Central China Development Company. Both these companies have been called "national policy" companies. They are to act as holding companies for the various subsidiary firms which either have been or will be called into existence. Examples of such subsidiaries are the North China Communications Company and the North China Telegraph and Telephone Company. How far this policy, which is obviously based on the example of the South Manchuria Railway, will be successful, remains to be seen, but it appears most unlikely that the Japanese will be able to produce for some time the vast amount of money which is needed to finance these companies.

228. The Chinese Government have equally had to impose trade restrictions, but in their case these were legitimate methods of defence. The Foreign Trade Commission, established at the end of 1937, aimed at the promotion of the export trade to obtain the maximum amount of foreign exchange possible in order to finance China's imports of munitions and other supplies. In March 1938, after the Japanese had set up the Federal Reserve Bank in the north, exchange control became essential, and as a result exporters in Hankow were informed that increased transportation facilities would only be available on the Canton–Hankow Railway if the bills of exchange for the produce had been sold to the same banks. The exporters had no alternative but to comply, and, in view of the limited facilities provided by this one railway, their requirements were met as well as could be expected.

229. In view of their importance to the national economy, the Chinese Government were impelled to resort to state trading in certain commodities such as wood-oil, tea, antimony, wolfram and bristles. The operations of the Fu Hua Trading Company, which was the official selling organ of the Foreign Trade Commission, were not always satisfactory to foreign merchants, and many of their actions, such as buying at high prices from producers, selling at low prices abroad and making up the difference by profits on other operations, were calculated to drive foreign merchants out of business.

230. Informal representations were made on various occasions against this kind of unfair trading, which was sometimes aggravated by suspicions of official corruption, but, in view of the vital necessity of foreign trade to the Chinese Government and its value in prolonging China's resistance, it was generally thought wiser to accept the situation and make the best of it.

Shipping.

231. Conditions on the coast and for river shipping have been more disturbed during the last year than for many years past. In spite of this, British shipping has succeeded in maintaining its percentage of the total amount

21

of shipping done. This is due, however, largely to the elimination of the Chinese, whose ships have either been sunk to form booms, or captured by the Japanese, and also to the fact that the Japanese have needed so many ships for their military requirements that they have had very few left for the China trade.

- The chief problem at the moment is the question of the reopening of the Yangtze River to third-Power shipping. As early as last March British shipping firms began to press for the free navigation of the river up to Kowan (below Chinkiang) at least, on the grounds that the dangers to navigation on which the Japanese laid such emphasis were largely illusory, and also that their trading would in no way interfere with the course of military operations. At that date the Japanese had perhaps some justification for their plea of military necessity in keeping the river closed, but as the months went by and as hostilities moved further up the river this argument began to grow threadbare. Moreover, in spite of repeated denials, it became obvious after August that Japanese vessels were using the river freely for purposes of trade. At the beginning of November parallel representations were made by both His Majesty's Government and the United States Government against the continued closure of the river. The Japanese Government replied that all Japanese vessels on the Yangtze were used for military purposes, and that they were not trading. In spite of this statement, it remains true that Japanese vessels were still trading freely to Wuhu and beyond at the end of the year.
- 233. At Tsingtao the Chinese sank a boom across the inner harbour before they left. This boom the Japanese have gradually removed, but they refuse to relax their restrictions on foreign ships entering the inner harbour, which Japanese commercial vessels use regularly. On the plea of military necessity, British and other foreign ships have been kept waiting in the outer harbour, and have been forced to load and unload their cargoes on the beach by the use of lighters under most unfavourable conditions. The establishment of monopoly lighterage companies, under Japanese control, both here and at Chefoo, has rendered the situation still more difficult for British shipping. The services performed by these companies are both expensive and inadequate, and it is scarcely surprising to find that many firms have had to ship their cargoes by Japanese vessels, which have access to the wharves. Repeated protests, both locally and at Tokyo, have had no effect. The Japanese naval mission shows no inclination to abate its restrictions in any way.
- 234. In Central China the Japanese have instituted a company to monopolise all inland river shipping. The company started as the Kiang-Che Shipping Company, and later became the Shanghai Inland Waters Steamship Navigation Company, under the control of the Nisshin Kisen Kaisha. Its object was to compel all shipowners to take shares in the concern, by contributing their ships. The amount of shares held by any individual was to be determined by the Japanese valuation of his ships. The scheme has, however, hitherto met with scant success, owing to the opposition of both Chinese and foreign shipowners.
- 235. At the mouth of the Pearl River the Chinese sank yet another of their booms, and on the capture of Canton the same difficulties arose over the opening of the river as occurred on the Yangtze. The river is still closed, and it appears likely that the Japanese will attempt to treat the problem as ancillary to that of the Yangtze (and the harbour at Tsingtao) in the hope of extorting greater concessions thereby.

Railways.

236. At the beginning of the year the Japanese were already in control of the majority of the railways in China. In the north they held the Peking-Mukden, the Peking-Suiyuan, part of the Peking-Hankow, the Tatung-Taiyuan, the line from Taiyuan to Shihchiachuang, and the Chiaotsi (Tsingtao-Tsinan) Railway. Further south they held the Shanghai-Nanking Railway, the Shanghai-Hangchow section of the Shanghai-Hangchow-Ningpo Railway, and both ends of the Tientsin-Pukow line. As a result of their military efforts during the year, they now control, in addition, all the Tientsin-Pukow Railway, the Lunghai Railway from the sea to Kaifeng, all the Peking-Hankow, with

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the exception of a section south of the Yellow River, both ends of the Canton–Hankow line, and the Canton–Kowloon. They have also captured the whole of the Taiyuan–Puchow line in Shansi. Thus, of the railways existing before the hostilities, the Chinese Government is left with only the Yunnan Railway to Indo-China and the Chekiang–Kiangsi line from Hangchow (the rails on the Kiukiang–Nanchang Railway were taken up before the Japanese arrived).

- 237. Through traffic on most of the lines held by the Japanese has now been restored, with the exception of the Tientsin-Pukow line, where the Huai River bridge has not yet been repaired. The Shanghai-Nanking Railway and the Shanghai-Hangchow Railway have been opened to passengers and freight since the early summer, and they have been remarkably free from guerrilla interference. In the north, however, the Japanese have not been so fortunate, and the cutting of one or more railways has been a regular occurrence. Railways, however, are difficult to blow up entirely, and the guerrillas, who are handicapped by a lack of explosives, have not always been as successful as they might.
- 238. The Japanese have made it clear that they propose to deal with the railways they have captured as they think fit, and have paid scant regard to the foreign interests in the various lines they hold. They have steadily refused permission for the representatives of the foreign bondholders to inspect either the Shanghai–Nanking Railway or the Shanghai–Hangchow Railway. They have forced the foreign staff of the Peking–Mukden line to become mere cyphers, and they have built a railway from Jehol to Tungchow without regard for the provisions of the agreements of 1898 and 1902. Finally, by the establishment of a North China Communications Company, under the North China Development Company, to take over the control and co-ordination of all railways in North China, they have shown that such activities are not dictated purely by military considerations, or "the need for restoration of railway efficiency," but form part of their plans for the development of the north, and are scarcely likely to be altered by representations alone.
- 239. The Chinese Government, in their efforts to develop the south-west and to find new routes to replace those they have lost, have paid considerable attention to railway construction. The Siang–Kwei line from Hengyang to Kweilin is now reported to be open for traffic, and certainly the progress which had been made on it by last August suggests that it should be ready. It is proposed to continue this line to Nanning, and from there to Langson across the frontier in French Indo-China. Good progress has been made on the southern section from Nanning to Langson also, and the bed is said to be now prepared.
- 240. Unfortunately, the Chinese Government is seriously handicapped in its efforts by a shortage of construction materials. The building of the Chungking-Chengtu Railway has been stopped for this reason, and some of the material intended for it has been diverted to the Siang-Kwei line. The same is true of the projected line from Chuchow to Kweiyang, on which progress has also been stopped.
- 241. Further plans for a Burma-Yunnan Railway and a railway from Chengtu to Yunnan have been under discussion for some time and are referred to in paragraph 163 of this report.

Customs Administration.

242. The preservation of the integrity of the Chinese Maritime Customs Administration as an efficient and independent service with a fair proportion of foreign staff, has always been regarded as an important British interest, in view both of the leading part played by British subjects in its development and of its importance to China's credit structure. Japanese attempts to gain control of the Customs in the occupied areas on behalf of their puppets were accordingly closely watched by His Majesty's Government in the United Kingdom. The first step taken by the Japanese during the year was the introduction in North China on the 22nd January of the new tariff, which, as recorded in last year's report, had been prepared by the Peking Provisional Government late in 1937.

This was accepted by the customs under force majeure, since it was feared that failure to comply would precipitate the seizure of the customs in the occupied areas by the Japanese. Pressure continued, however, chiefly on account of the desperate need of funds experienced by the puppet Governments at Peking and Nanking. It was feared that this might result in action being taken at Shanghai to secure Japanese control of the customs there. Protests having proved unavailing, His Majesty's Ambassador in Tokyo accordingly negotiated with the Japanese Government regarding a method of securing the interests of the foreign bondholders in the customs, in the hope of thereby averting the break-up of the administration. An agreement for this purpose was signed on the 2nd May. It provided that customs duties collected in the occupied ports should be deposited in the Yokohama Specie Bank, and that funds should be released from this account to meet administrative expenses and to provide proportionate quotas for the service of foreign loan obligations secured on the Chinese customs revenues. The Japanese insisted, however, that the Chinese should agree in return to release all funds collected at occupied ports since the date of the Japanese occupation, and, further, that the Chinese Government should pay the Japanese · Boxer Indemnity, which had been withheld since September 1937.

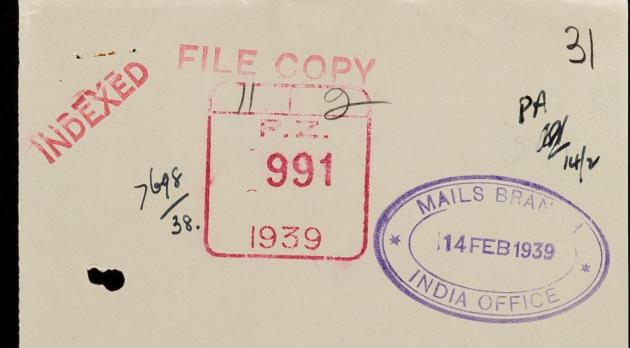
- 243. The Chinese Government refused to accept the agreement, which accordingly did not come into force. No revenue collected at ports under Japanese occupation was therefore made available for the service of foreign or domestic loans.
- 244. Soon after the signature of the customs agreement the Japanese, acting in the name of the Peking and Nanking Governments, introduced a new tariff, substantially lower than the previous tariff, in all ports under their control. This tariff also was duly enforced by the customs, who were permitted in return to resume control of Japanese and Chinese wharves in Shanghai with the result that there was a considerable reduction in smuggling. Smuggling was also greatly reduced in the notorious East Hopei area during the course of the year. These improvements were only secured, however, at the expense of concessions to persistent Japanese demands for the recruitment of additional Japanese staff. The inspector-general was prepared to meet such demands within reason, but they were resisted whenever they appeared likely to reduce the efficiency of the Customs Service as a whole. In some cases, as at Amoy, Chefoo and Tsingtao, these demands were accompanied by virtual blackmail in the form of seizure of customs vessels and other property and the refusal to return these until the Japanese demands were granted. The Inspector-General of Customs was given all possible support by His Majesty's Government in his delicate task of maintaining the integrity of the administration in these difficult conditions.

Salt Administration.

- 245. The Salt Administration, founded in 1913 with British assistance and still employing a number of British officials, stands next in importance to the customs as a mainstay of China's finances and security for her foreign loans. During 1938 it has been in a state of disorganisation. As early as March areas normally producing more than half of the total salt revenues had passed out of the control of the Chinese Government. On the other hand, only one important salt-producing area was effectively occupied and exploited by the Japanese. There has been considerable criticism in this connexion on the part of senior foreign officials directed against the policy of the Ministry of Finance and the (American) co-director-general, who have withdrawn all staffs from the areas affected by the hostilities. The foreign officials argue that reporting and liaison officers could be sent back to some of the areas in question and that they might be able to re-establish a measure of control and collect some revenue, without exceeding their authority or being obliged to have compromising dealings with the Japanese. Discussions were proceeding on these lines at the end of the year.
- 246. Suggestions have been made from time to time that with a view to preventing the disintegration of the Salt Administration and safeguarding the service of the foreign loans secured on the salt revenues, His Majesty's Government should lend their good offices in negotiating with the Japanese Government an agreement on the lines of the Customs Agreement of the 3rd May (see paragraph No. 242). The Chinese Government were at first unwilling to agree to

such negotiations, but their attitude changed after their decision in September to defer amortisation on two salt loans. In October, His Majesty's Ambassador informed them that, while His Majesty's Government were willing to lend their good offices, they could see no prospect of negotiations succeeding so long as the Chinese Government refused to allow the customs agreement to come into force.

247. In August the Japanese Government renewed their assurances that they would fully respect the interests of His Majesty's Government in the Chinese Salt Administration. They have made no attempt to implement this promise, and indeed one of the functions of the North and Central China Development Companies (see paragraph No. 227) has been declared to be the production and marketing of salt.



WITH THE COMPLIMENTS

OF THE

Reference Freign Office letter No. 1354 85 405 of February 22-3

Foreign Office,

February 13, 1939

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ANNUAL REPORT, 1937.

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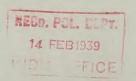
IN paragraph 179 of the report it is stated that:-

"The Australian delegation to the conference at Brussels on the Far Eastern crisis was instructed by His Majesty's Government in the Commonwealth of Australia to oppose anything in the nature of sanctions against Japan."

This paragraph does not indicate correctly the attitude taken up by the Commonwealth Government at the time of the conference and is not in accordance with the instructions issued to the Commonwealth delegate. The position of the Commonwealth Government was laid down in a telegram to the Secretary of State for Dominion Affairs, dated the 28th October, 1937, the concluding paragraph of which read:—

"The Commonwealth Government feels that it cannot at this stage commit itself to any course beyond that of conciliation and agreement. If, however, the conference feels itself impelled to discuss other measures and to make definite proposals or recommendations, they should be submitted to the League through the Advisory Committee, which will afford the Governments an opportunity for further considering the position."

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Notes.

Minute Paper.

Register No. P. Z.7698 38.

SECRET.

POLITICAL DEPARTMENT

Dated

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	Date.	Initials.	SUBJECT.
Under Secretary Secretary of State Committee Under Secretary Secretary of State	5.12	2004.	China Annual Report for 1937

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FOR INFORMATION.

Of direct interest to this Office are: -

Paras 76-83. Sinking

Paras 84-87 Tibet

Paras 180-183 Burma

Of general interest: -

Paras 69-75 Mongolia

Paras 88-142 Military Operations

Paras 308 - 325 Aviation (military)

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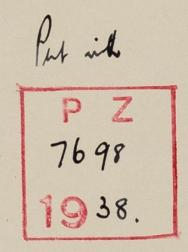
POLITICAL COMMITTES

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WITH THE COMPLIMENTS

OF THE

UNDER-SECRETARY OF STATE FOR FOREIGN AFFAIRS.

Reference Foreign Office letter No L 1354/ 85/408 of Following 222

Foreign Office,

December 12, 1988.

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CHINA.

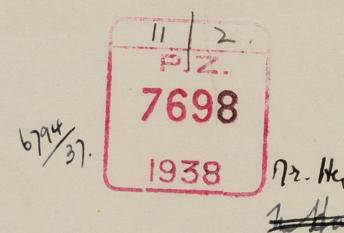
ANNUAL REPORT, 1937.

LIST OF CORRIGENDA.

- Paragraph 34. For "Luokouchiao" (line 1) read "Lukouchiao."
- Paragraph 42. After "furious" (line 10) insert "air."
- Paragraph 129. For "brought" (line 4) read "bought."
- Paragraph 168. For "November" (line 2) in both places read "December."
- Paragraph 197. After "paragraphs" insert "60-68."
- Paragraph 225. After "paragraph" insert "182."
- Paragraph 239. For "Chaitung" (line 9) read "Chaitang."
 - For "Canton" (line 19) read "Kwangtung."
- Paragraph 250. For "Chamber" (line 17) read "Chambers."
- Paragraph 255. For "peservation" (line 5) read "preservation."
- Paragraph 279. After "appeared" (line 4) delete "that."

Far Eastern Department, November 30, 1938. MOEXED

36



WITH THE COMPLIMENTS

OF THE

UNDER-SECRETARY OF STATE FOR FOREIGN AFFAIRS.

Reference Foreign Office letter. No. L 1354 85 405 of February 22? 1926.

Foreign Office, November 17, 1938.

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INDIA OFFICE

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CHINA.

ANNUAL REPORT, 1937.

[F 6312/6312/10]

Sir A. Clark Kerr to Viscount Halifax.—(Received June 13.)

(No. 223.) My Lord, Shanghai, April 29, 1938.

WITH reference to Sir Hughe Knatchbull-Hugessen's despatch No. 368 of the 8th April, 1937, I have the honour to transmit to your Lordship herewith the annual report on China for the year 1937. I am indebted for the preparation of this report, in the face of considerable difficulties, to the members of the staff of this Embassy, at Peking as well as at Shanghai.

I have, &c. (In the absence of the Ambassador) J. D. GREENWAY.

Enclosure.

Annual Report on China for 1937.

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I.—INTERNAL POLITICAL SITUATION.

General (including Sino-Japanese Relations).

THE Sian coup had taken place on the 12th December, 1936, and the generalissimo had been released and had dramatically returned to Nanking in company with his captor on Christmas Day. The Young Marshal, who had thrown himself on the mercy of the Government, was tried by a military tribunal and sentenced to ten years' imprisonment and deprivation of civil rights. This was, however, a mere gesture intended to assert the authority of the Central Government, and it was followed almost immediately by a free pardon.

- 2. But though the incident itself was thus closed, the political issues involved were still outstanding, and a plenary session of the Central Executive Committee of the Kuomintang was summoned for the 15th February to consider these issues. This allowed time for tempers to cool and some *modus vivendi* to be arranged. Meantime, the generalissimo's resignation was tendered and refused three times as required by Chinese custom, and he was then given one month's leave—subsequently extended by another fortnight—and returned to his home near Ningpo to tend his injuries, which time showed to be more serious than was at first supposed.
- 3. The release of the generalissimo (and of the other officials who were arrested at the same time), though it alleviated the anxiety at Nanking, did not immediately alter the situation in the north-west, and for some time the Central Government forces and the rebels remained facing each other while negotiators and intermediaries went back and forth between Nanking and Sian. Eventually, however, an understanding was reached whereby General Yang Hu-cheng's provincial troops and the North-Eastern armies were to withdraw to agreed positions and Sian was to be occupied by the Central Government forces without opposition. The decision to withdraw was hotly opposed by the Communists and the Radical elements in the rebel forces, as it was the death-blow to the common front, and disorders occurred in Sian on the 2nd February which involved the murder of four of the senior officers in the North-Eastern Army. Nevertheless, the arrangement was faithfully carried out, and in the first days of February the Central Government troops advanced without opposition and occupied Sian while the North-Eastern and provincial forces withdrew westwards and northwards to the positions agreed upon.
- 4. The Communist forces, which had come down from the north-west and had occupied a number of towns in Central and Southern Shensi, withdrew simultaneously and unmolested into the north of the province.
- 5. Meanwhile, Mr. Wang Ching-wei, who had been recuperating in Europe from the effects of the attempt on his life on the 1st November, 1935, had hurried back to China at the first news of the generalissimo's arrest, and had hardly landed in Shanghai on the 18th January before he began a slashing attack on the Communists and the "common front." Mr. Wang was one of the two remaining members of the Standing Committee of the Central Political Council (General Chiang Kai-shek being the other). By virtue of his position as well as of his personal popularity and prestige he carried great weight in the party, and his return had a steadying effect on those who were beginning to wonder if there was not after all something to be said for the "common front against Japan."
- 6. The plenary session of the Central Executive Committee opened at Nanking on the 15th February and lasted eight days. There was a large attendance, but it was noticed that almost every one of the old-style provincial barons absented himself on one excuse or another: Yen Hsi-shan of Shansi, Han Fu-chu of Shantung, Sung Che-yuan of Hopei-Chahar, Liu Hsiang of Szechuan, and Li Tsung-jen of Kwangsi. Pains were taken to make it appear that this was a routine half-yearly session, and a large number of reports and resolutions on all phases of the national life were considered, but, in fact, the only issues to which serious attention was given were those of Sian and the Government's attitude towards the Communists. The Chinese Communist party had tabled a programme in five points, as follows:—
 - (1) Suppression of civil war and concentration of all national strength for single-minded resistance to external aggression.

(2) Freedom of speech, assembly, organisation, &c., and release of all political prisoners.

(3) Convocation of a congress of all parties, factions, military groups and organisations in order to concentrate national talents for the salvation of the country.

(4) Immediate accomplishment of the preparatory work for a war of resistance against Japan.

(5) Amelioration of the living conditions of the people at large.

- In consideration of the adoption of a programme on the foregoing lines, the Communist party undertook-
 - (1) To abandon its attempts to overthrow the National Government by force;
 - (2) To transform the "Soviet Government of China" into the "Government of the Special Region of the Republic of China," and the "Red Army" into the "National Revolutionary Army" under the direct leadership of the Central Government and the Military Affairs Commission;

(3) To enforce a complete democratic system of universal suffrage within the "Special Region"; and

- "Special Region"; and
 (4) To abandon the policy of expropriating the land of the landlords, and to follow loyally the programme of the anti-Japanese united front.
- General Chiang Kai-shek did not himself attend the meetings of the plenary session, but he submitted a long written statement on the events at Sian, which was read at the meeting of the session on the 19th February. In this he recounted how the Young Marshal and his associates had attempted to force him to accept the eight-point national salvation programme and how he had replied that if the Young Marshal had any proposals to make he should submit them to the Central authorities in the recognised way, but that he himself would not only not submit them on his behalf but would oppose them as he did not consider them in the interests of the State. The plenary session, after congratulating the generalissimo on the courage and resourcefulness which had brought both himself and the country through a dangerous crisis, went on to make short work of the eight-point programme which, since it had been submitted through rebellious action and by means of pressure, must, it was decided, be refused consideration regardless of its contents.
- 9. The question of the relations of the Government and party to the Communists was dealt with both in a special resolution and in the session's final manifesto. The history of Communist activities in China was reviewed at some length; it was shown how the Communists had burrowed inside and undermined the Kuomintang and aggravated and taken advantage of every national emergency and the conclusion was reached that the present overtures for surrender were dictated not by patriotic motives but by the extremity in which the Communists found themselves. While, it was declared, the Kuomintang was prepared to readmit any persons who sincerely repented their faults, there could be no compromise with communism, which was the enemy of the State and must be cut off root and branch. With specific reference to the Communist five-point proposals and promises, the "minimum requirements" of the plenary session were: complete abolition of the so-called "Red Army" and any other Communist armed forces under whatever name; complete abolition of the so-called "Soviet Government" and all other organisations detrimental to national unity; and absolute cessation of Red propaganda and class strife in any form.
- While thus declaring in the clearest language the firm resolve of the Kuomintang and the Government to have no truck with communism, the common front or "national salvationism," the plenary session at the same time had to take account of the feelings which were responsible for these movements; dissatisfaction with the Government's foreign policy, the lack of progress in political development at home, and the general economic distress. The manifesto insisted that the Government had in domestic issues been following a policy of forbearance and in foreign affairs a policy of non-toleration of aggression and non-conclusion of any agreement detrimental to China's territorial sovereignty; it had stood firm [17683]

on this policy in its diplomatic negotiations with Japan to the verge of a complete breakdown in the negotiations; the session saw no need to revise this foreign policy, and China would continue to work for the readjustment of Sino-Japanese relations on the basis of equality, reciprocity and mutual respect for each other's territorial integrity. The manifesto also announced that the National People's Assembly, postponed from last November, would be convened on the 12th November to adopt the Constitution and inaugurate the new régime of democratic government.

- 11. The resolutions passed at this conference were in effect a vote of confidence in the generalissimo and a confirmation of his policy of non-co-operation with the Communists, but the actual administrative and political problems were left for the generalissimo to solve, with little assistance except the Central Executive Committee's good wishes. Unfortunately, the generalissimo was not in a fit condition of mind or body to deal effectively with such problems. The spinal injury which he had sustained at the time of his capture turned out to be more serious than was at first supposed, and, in addition, he was suffering from poisoning which was eventually traced to his teeth. His physical troubles reacted on his temper—never one of the easiest—and according to those nearest to him it became almost impossible to get him to consider any question of State calmly and dispassionately. His six weeks' sick leave was extended by a month and again by two months, up to the end of May.
- 12. Nevertheless, considerable progress was made. After long negotiations, the various units of the disaffected North-Eastern Army allowed themselves to be transferred from Shensi and Kansu to the three key provinces of Honan, Anhui and Kiangsu, where they were to be reorganised as an integral part of the Central Government forces, but under their own officers; General Yang Hu-cheng, former commander of the XVIIth Route Army and one of the leaders of the Sian coup, was induced to resign, and his place was taken by General Ku Chu-tung, one of the generalissimo's most trusted men, under whom the Central Government's control over the centre and south of Shensi Province was consolidated.
- 13. On the 8th March Dr. Wang Chung-hui assumed the post of Minister for Foreign Affairs, in place of General Chang Chun, and he was subsequently appointed acting president of the Executive Yuan during the generalissimo's absence. This was the only change of any importance which might be construed as a gesture of conciliation towards the more extreme anti-Japanese elements in the country.
- The Japanese had been watching these events with intense suspicion, and they were even now only half persuaded that Chiang Kai-shek had not made terms with the Communists and that the whole Sian affair and the session of the Central Executive Committee were not parts of a comedy intended to hoodwink them and lull them into a sense of false security. It must be admitted that their suspicions were not altogether without foundation since it became known that the Communist leaders were holding secret and unofficial conversations not only with representatives of the Central Government but even with the generalissimo himself. Nevertheless, for a time, the tension between the two countries eased. There was even talk in Japan of a reorientation of the Japanese China policy on a basis of equality and compromise. General Hayashi, in his opening address to the Diet on the 15th February, spoke of fostering mutual appreciation and cultivating cordial feelings between China and Japan. The Minister for Foreign Affairs, Mr. Sato, startled the House of Peers on the 8th March by voicing the novel theory that negotiations with China should be conducted on a basis of equality and in a conciliatory spirit. A Japanese economic mission visited China in March under the leadership of Mr. Kenjo Kodama. "We are going to China to shake hands with the Chinese people," Mr. Kodama announced. But it was evident that the Japanese had not in fact abated one jot of their ambitions in China; but that they had decided to drop for the time being their *political* demands as unrealisable in existing conditions, and to concentrate on the development of their *economic* position in North China. The Chinese were wide awake to the implications of this change of tactics and made it clear that they did not intend to be humbugged by any "friendship drive" into accepting the status quo which the Japanese had forced upon them. Mr Kodama and

his mission were told that the removal of political obstacles, particularly the abolition of the East Hopei régime and the suppression of smuggling in North China, must precede any economic rapprochement.

- 15. The Japanese allowed it to be understood that in certain circumstances and on certain terms the East Hopei organisation might cease to exist and the smuggling might be put down. But the Chinese would not listen to any suggestion of the kind. General Chiang Kai-shek told His Majesty's Ambassador that Japan must first settle the East Hopei, North Chahar and smuggling questions; then and not till then an atmosphere would be created in which the Chinese could discuss such matters as economic co-operation in the north.
 - With the Chinese and Japanese points of view so widely separated, there seemed little hope of any early improvement in Sino-Japanese relations. The tendency was rather in the other direction, since on the one hand the Chinese were gradually taking a stronger line in the numerous disputes which arose with their neighbours, and on the other hand the Japanese, exasperated by the refusal of the Chinese to meet their advances, were pushing ahead with their development schemes in North China without paying any attention to the Chinese protests. The Chinese, emboldened by the belief that the Japanese were prevented by affairs at home from embarking on any foreign adventure, had, indeed, gone further than they would have dared a few months earlier. Reference has already been made to the transfer of the former North-Eastern troops to Kiangsu, Anhui and Honan. This move, which placed some of the most anti-Japanese forces in China in a position where they would be in the van of any conflict with the Japanese in the north, was, of course, construed by the Japanese as an unfriendly act. Then the Chinese, in defiance of Japanese objections, transferred a large force of armed revenue guards into the Tsingtao area, where their presence was, in the Japanese view, undesirable. "China," said General Sugiyama to the Prefectural Governors assembled in conference at Tokyo on the 19th May, "is tending to feel over-confident of her strength; this tendency is causing her to change her anti-Japanese attitude to one insulting to Japan."
 - 17. Nevertheless, there was nothing in the situation to cause alarm, and even experienced observers were taken by surprise by the events which so soon supervened. While it was common knowledge that all Chiang's energies were bent towards preparing the Chinese people for a war of resistance against Japan, it was also common knowledge that he was counting on having another two years in which to prepare for this supreme test of strength. As for the Japanese, it was felt that they would be unlikely to force an issue with China while their relations with Russia were so strained.
 - 18. On the 1st June the generalissimo announced that his health was restored and that he was resuming his duties.
 - On the 7th July occurred the Lukouchiao incident, an affair unimportant in itself, but disastrous in its repercussions. At the time of the incident the Japanese forces in and near Peking consisted of one battalion, about 550 strong, at Fengtai, and the Embassy guard, about 450 strong. The Chinese forces consisted of units of the 37th and 38th Divisions of the XXIXth Army, with other miscellaneous troops and gendarmerie, more than 15,000 in all. A portion of the Japanese garrison at Fengtai was engaged in night manœuvres at Lukouchiao, when shots rang out. Believing themselves to be attacked by the Chinese forces, of which there were considerable numbers in the neighbourhood, the Japanese hurriedly brought up reinforcements and demanded that they be allowed to enter and search the walled city of Wanping for the culprits. Chinese refused, and on their side brought up reinforcements, and though Chinese and Japanese officials intervened and endeavoured to settle the incident locally and immediately, it seemed that a mechanism had been set in motion which it was impossible to arrest. As fast as truces could be arranged they were broken, each side charging the other with bad faith. In the meantime, alarming reports were reaching both Tokyo and Nanking regarding the extent and implications of the conflict, and of the military measures which each side was alleged by the other to be taking. By the 11th July all available men from the Tientsin Japanese garrison had been sent to Fengtai, and reinforcements were beginning to arrive from Manchukuo. On the Chinese side units of the XXXIInd, XLth

and LIIIrd Armies, already stationed in Hopei, began to concentrate towards Shihchiachuang and Paoting (Peking-Hankow Railway), whilst three divisions of the XXVIth Route Army were ordered to move from Hupeh to Paoting. On the 11th July the Japanese Cabinet met in extraordinary session to consider "fundamental decisions" said to have been reached with regard to the Government's North China policy, and a Cabinet communiqué announced that the Government was taking all the necessary measures for the despatch of military forces to North China, though it was still hopeful that an amicable solution might be reached, and the affair localised.

- 20. The Chinese authorities were also anxious to localise the incident, and there can be no doubt that their anxiety was increased by the extent of the Japanese military preparations which were now becoming evident. Late in the evening of the 11th it was announced that an agreement had been reached for the settlement of the incident, and that—once more—both sides were to withdraw. The terms of this agreement have never been officially published, but were to the following effect:—
 - (1) Withdrawal of Chinese troops from the Wanping area and their replacement by gendarmerie.

(2) An apology to be tendered on behalf of the XXIXth Army, and those persons responsible for the incident to be punished.

(3) Appropriate measures to be taken for the suppression of "Blueshirt," Communist and anti-Japanese activities.

- 21. This last was a sort of omnibus clause under which the Japanese military authorities could demand the removal of any person and the suppression of any form of activity which they might dislike. As a first step they demanded the removal from the Peking area of the 37th Division, which they regarded as particularly anti-Japanese. This demand caused great indignation among the Chinese, but General Sung Che-yuan decided that discretion was the better part of valour, and the withdrawal of the 37th Division to points further south along the Peking–Hankow line was begun.
- Meanwhile, the Central Government were much disturbed at the turn which events in the north were taking. Sian had shown that there were important elements of the nation which would no longer put up with a temporising policy in face of continued Japanese encroachments, and General Chiang Kai-shek himself was under a pledge to resist any such encroachment by force. Feeling in the country was greatly excited, and it seemed clear that if he did not fulfil his pledge he would have to give up the leadership to bolder spirits. With a heavy heart and a clearer appreciation of the consequences than his critics, he chose the former course and arranged for the transfer of certain Central Government divisions to positions where they could, if necessary, support the XXIXth Army. The Japanese, as was expected, regarded the movement as provocative and demanded their withdrawal. Diplomatic exchanges took place at Nanking, which only defined the essential point of difference more clearly, namely, that the Japanese military authorities were determined to deal directly with the North China officials, whom they chose to regard as autonomous, while the Central Government were determined to assert their own authority and allow no more local settlements of national questions.
- 23. Encouraged by the signs of Central Government support General Sung Che-yuan tried to play for time. But on the 24th July the Japanese presented an ultimatum demanding the withdrawal of the 37th Division from one area by noon on the 29th and from another by noon on the 28th. General Sung issued a proclamation announcing that it was impossible for him to accept the Japanese demand. Consequently the Japanese troops on the 27th July began to carry out their threat to evict the 37th Division (and the 132nd Division which had in the meantime been included in the interdict as the result of a clash which had taken place between units of that division and Japanese troops on the preceding day). Heavy fighting ensued all round Peking, but the Japanese, immensely superior in armament, made short work of the Chinese resistance, and by the evening of the 28th all units of the XXIXth Army in Peking and neighbourhood were in full retreat. Hostilities broke out almost simultaneously at Tientsin, where units of the 38th Division (which the Japanese had come to regard as "safe")

and gendarmerie made a surprise attack on the Japanese garrison. The Japanese, though taken off their guard, reacted with characteristic vigour, and within twenty-four hours had the situation under control, but by that time the Nankai University and other important buildings were in flames, and enormous loss of Chinese life and damage to property had occurred. The foreign concessions were for a time in great danger, but miraculously escaped with but few casualties.

- 24. All hope of a peaceful solution now vanished. On the 29th the generalissimo sent a message to His Majesty's Ambassador that the Government was now going to fight to the bitter end. The decision once taken, such dispositions as the imperfect political and military organisation of the Government permitted were put into effect. As soon as it was realised that the generalissimo was this time really taking up the Japanese challenge all parties rallied to his support. Han Fu-chu, Yen Hsi-shan, Liu Hsiang, Yu Han-mou all came to Nanking to discuss arrangements and troop dispositions; what was more important, they placed their forces at the disposal of the Central Government for the common purpose, and one saw—a strange phenomenon in China—Szechuen troops in Hupei and Kwangsi troops in Shantung, not as invaders, but as partners in a common enterprise. Most important of all, perhaps, General Pai Chung-hsi, the inveterate enemy of General Chiang Kai-shek, at last buried the hatchet and came to Nanking. After the generalissimo, General Pai was the most trusted figure in China. He was in popular estimation the best strategist in the country, and the news that he was not only going to remain in Nanking, but was to take up the post of vice-chief of the General Staff under General Cheng Chien was hailed with a sigh of relief.
- 25. The Communists had already indicated their intention of supporting the Government in the event of war against Japan. The issue now being joined, there was no more need to keep them at arm's length: their help might indeed be invaluable. All Communist and other political prisoners were released, Communist leaders were taken into the counsels of the Government, and the Communist armies, which had for so many years been warring against the Kuomintang, were given status as a national army. In return the Chinese Communist party declared its abandonment of purely Communist principles and its allegiance to the Kuomintang in the task of fighting Japan.
- 26. Though a common front was established, the unity hardly went below the surface. The jealousies and mutual suspicions of the various provincial militarists could not be broken down in a day, while the difficulties arising from the feudal organisation of the national forces and the failure to build up a national general staff in time of peace proved insurmountable. These were, as much as actual military unpreparedness, the prime cause of the disasters which ensued.
- 27. The Japanese followed up their occupation of Peking and Tientsin by a drive for Kalgan to secure the Peking–Suiyuan Railway, the control of which was all-important to them for the protection of their flank both from Soviet Russia and from the Chinese forces in the north-west. They began their drive along this line by an attack on the Chinese positions in the Nankou Pass on the 2nd August. By the end of the month they were in control of Kalgan and the whole of South Chahar. Advancing westward they occupied Paotou, the terminus of the Peking–Suiyuan Railway, and having thus secured their flank, they turned southwards, and advancing along the three railway lines, the Tientsin–Pukow, the Peking–Hankow and the Tatung–Puchow lines, at great speed they made short work of the numerically much superior, but militarily much inferior Chinese forces which attempted to oppose them.
- 28. The fundamental policy of the Japanese was to concentrate on the north and to avoid being drawn into expensive and strategically useless sideshows in other parts of China. They had accordingly at first intended to withdraw their communities from all except a few of the more important centres, such as Hankow and Tsingtao, but, as they felt the strength of the hostility against them and realised the danger of massacres, they reluctantly withdrew even from these centres until the whole of China south of the Tientsin–Peking zone had been completely evacuated by Japanese nationals and officials, with the single exception

of Shanghai. The situation at some of the ports was for a time exceedingly tense. At Hankow the small Japanese Concession was to all intents and purposes invested by a large Chinese army. It was impossible for the Japanese to defend it, and it was only the tardily reached and hastily executed resolve to evacuate it completely that averted a tragedy.

- 29. At Tsingtao a crisis was precipitated by the shooting of two Japanese sailors by an unidentified assailant on the 13th August. Urgent representations were made by the representatives of the principal Powers both in Nanking and Tokyo to prevent this seaside resort from becoming involved in hostilities and eventually the Japanese Government, to the general relief, decided to evacuate the port completely. Japanese mill and other property, estimated by the Japanese to be worth 300 million yen, was handed over to the custody of the Chinese authorities.
- 30. All this took time. The evacuation of Hankow was completed on the 11th August, that of Amoy on the 28th August, and that of Tsingtao only on the 4th September.
- 31. Meanwhile most serious developments had taken place at Shanghai. As the result of the 1932 Truce Agreement, the Japanese forces were withdrawn inside the International Settlement and Chapei "salient," while the Chinese undertook to remain outside the line to which they had been driven by the Japanese "pending further arrangements," the intervening area to be policed meanwhile by a force of gendarmerie to be established by the Chinese for the purpose. Inevitably, the two sides, and the foreign friendly Powers who had participated in the truce conference, could not agree on the scope of the "further arrangements." The Japanese had envisaged a round-table conference at which all the international problems of Shanghai would be discussed; the Chinese maintained that the "further arrangements" dealt only with the restoration of peaceful conditions in the Shanghai area, whereafter the Truce Agreement lapsed, and they would have nothing to do with any round-table conference unless it dealt with Manchuria as well as Shanghai; and the foreign Powers, who had half agreed to the idea of a round-table conference, hastily drew back when it became evident that they were to be used for the purpose of exacting further concessions from China in the Japanese interest.
- 32. Thus Japan has always regarded herself as having been betrayed by the Powers, and, failing a fundamental solution by international agreement securing her position to her own satisfaction, has taken her own measures to assure the safety of her nationals. The marine landing force permanently stationed in Shanghai was greatly increased, fortress-like headquarters to accommodate 2,000 men as well as equipment and stores for several times that number were built, and night exercises covering the whole of the Hongkew and "salient" areas became a regular institution. Naturally even this force could not protect the Japanese residents, or even the landing force itself, from the activities of gummen and anti-Japanese fanatics, so that incidents were constantly occurring. Helpless to prevent such incidents, all the landing force could do—and did—when they occurred was to demonstrate in force, thrash around and make the situation as uncomfortable as possible for the wretched Chinese in the neighbourhood.
- 33. The Chinese argued that the military preparations being made by the Japanese went far beyond what was necessary for the defence of Japanese interests in the settlement, and could only be interpreted as evidence of an intention once again at the appropriate moment to use the Settlement as a base for operations outside. China's national spirit was growing, and there was a general determination that if there was another 1932 affair it should have a different result. Accordingly, and as an answer to the Japanese military preparations, the Chinese began unostentatiously to increase the numbers of the gendarmerie, provide them with machine guns and modern equipment, and other defensive positions were constructed in the truce zone, and even, so the Japanese alleged, the refortification of Woosung was begun. The Japanese became very uneasy at these preparations, which they alleged were a breach of the spirit if not of the words of the 1932 Truce Agreement, and in June 1937 they appealed to the Joint Commission (comprising representatives of the friendly

participating Powers as well as of China and Japan) for a ruling. The Powers, however, who regarded the Truce Agreement as an ad hoc arrangement for the settlement of a long-past emergency, and who had allowed the Joint Commission to be kept alive merely because it provided a useful buffer between the Chinese and the Japanese, were not prepared to support the Japanese thesis. The neutral members of the Joint Commission refused to express any opinion on the fundamentals of the Japanese complaint, and confined themselves to an enquiry to the Chinese side whether, as a gesture of conciliation and goodwill, they would be prepared to make any voluntary declaration as regards the composition and numbers of the gendarmerie in the Shanghai area, and/or on the question of any fortifications within the truce zone. This the Chinese refused to do and the matter was dropped.

- 34. At this moment the Luckouchiao incident occurred. Although at first the situation at Shanghai remained calm on the surface, the tensions below the surface began to increase. As hostilities in the North developed and the Japanese communities evacuated from the Yangtze ports began to arrive in Shanghai, these tensions became more and more acute. China and Japan were now virtually at war, and the Chinese forces in the Shanghai zone took up dispositions obviously arranged beforehand for such a contingency. The gendarmerie, which had grown into a well-armed force of at least 6,000, began to draw in towards the International Settlement, to build barricades on the outlying roads and challenge passers-by. Two, and possibly more, of the Central Government's best divisions were concentrated within easy distance of Shanghai. The Japanese became increasingly uneasy. They were undoubtedly anxious to avoid trouble at Shanghai, since their whole policy was, as mentioned in paragraph 28 above, to shorten their line and concentrate their effort in the North, instead of dissipating it in costly expeditions in other parts of the country. It was partly for this reason (partly also that effective protection was out of the question) that they were evacuating the Yangtze Valley. They were not, however, prepared to follow this policy to its logical conclusion by evacuating Shanghai as well; such an evacuation would, they felt, be too great a blow to their prestige.
- 35. The position of the Chinese was different; while it was greatly in their interest, too, to avoid trouble in Shanghai, the industrial and financial centre of the country, they were desperate and quite determined not to yield another inch to the Japanese, whatever the cost might be; and, of course, the more the Japanese effort was dissipated the better for China.
- 36. The seriousness of the situation was impressed on His Majesty's Ambassador when the Vice-Minister for Foreign Affairs told him on the 31st July that there might be disastrous consequences if the Japanese again used the International Settlement in Shanghai as a base for hostilities, since in such an event the Chinese might not exercise the same restraint as in 1932. His Excellency immediately consulted the Commander-in-chief regarding the possibility of obtaining an undertaking from the Japanese Government that neither the settlement itself nor the river fronting the settlement would be used in any way in connexion with hostilities. He was convinced, however, even then that it was the Japanese landing force which was attracting the danger to Shanghai, and he suggested that the only certain safeguard would be the complete withdrawal of the latter, in return, perhaps, for an undertaking from the other Powers to make themselves responsible vis- \hat{a} -vis the Japanese for the security of the settlement.
- 37. But it was already too late to avert the ensuing tragedy. And it may be said here, in parenthesis, that probably nothing that the Powers could have done, short of direct military action, would at any time have changed the course of events. The train was laid and only the spark was needed. There was a false alarm when on the 24th July a Japanese sailor disappeared from Shanghai in mysterious circumstances which suggested that he might have been murdered. After a preliminary flurry, however, the Japanese got their feelings under control, and the incident was turned off with an apology and a laugh when the sailor was found a few days later swimming in the Yangtze near Chinkiang, having apparently committed some offence against discipline and then run away to avoid punishment.

- 38. But the final conflagration was not long delayed. On the 9th August a Japanese sub-lieutenant of the landing force and a Japanese seaman acting as his chauffeur, both in uniform, were shot and killed on the Monument Road (the most outlying of the so-called extra-settlement roads in the Western District of Shanghai) in the vicinity of Hungjao Aerodrome. According to the Japanese version the officer was unarmed and was taking a motor drive in the ordinary way along a road where he had a right to be when the car was surrounded by gendarmerie who opened fire with machine guns and rifles. According to the Chinese version the officer was trying to force his way into the airfield, and when he was stopped by the guards he opened fire, killing some of the guards, whereupon the rest of the party returned the fire in self-defence. The Chinese version is certainly incorrect since it does not tally with the facts as subsequently ascertained; the Japanese version is incorrect because it is only half the truth. It can hardly be doubted that the officer was driving round by the airfield to see what information he could pick up; as much was subsequently admitted by the Japanese consul-general.
- The Mayor of Shanghai and the Japanese consul-general immediately met and agreed to settle the incident through diplomatic means. But the conditions of the problem were rapidly altering. On the 8th August, that is, on the day preceding the murder, the Chinese Government, through the Waichiaopu, had informed His Majesty's Ambassador and the other diplomatic representatives in Nanking that while the military authorities were anxious to maintain peace in and around Shanghai and entertained no intention of attacking the Japanese forces already there, they could not allow the Japanese to consolidate a position from which they could launch attacks on the Chinese forces, and that, accordingly, if the Japanese armed forces in Shanghai were augmented, the Chinese forces would "take the first opportunity to prevent them from disturbing peace and His Majesty's Ambassador and his American, French order in Shanghai." German and Italian colleagues, who were by now meeting in almost daily conferences, after consulting their respective Governments, addressed a joint note to the Japanese Ambassador on the 11th August informing him of the abovementioned communication and urging him to give an assurance that the Japanese authorities would do all in their power to exclude the Shanghai area from the scope of any possible hostilities. At the same time they addressed a note to the Minister for Foreign Affairs, referring to the communication which he had made to some of their number, informing him of the note which they were addressing to the Japanese Ambassador, and saying that they should welcome any additional assurances that the Chinese Government would do all in its power to exclude the Shanghai area from the scope of any possible hostilities.
- 40. Simultaneously, however, with the despatch of these representations the Japanese First Battle Fleet (minus battleships) appeared in Shanghai and additional marines were landed. The situation against which the Minister for Foreign Affairs had warned us on the 8th August had accordingly arisen. The Japanese consul-general at Shanghai at the same time notified the mayor that the gendarmerie forces, which were pressing the Japanese landing force at ancomfortably close quarters, must be withdrawn. He also appealed to the Joint Commission to find means to compel the Chinese to withdraw. The Japanese Counsellor of Embassy in Nanking likewise called on His Majesty's Ambassador and his colleagues to invoke their assistance in the same cause. But the Chinese were by this time in no mood to make any further concessions, and any suggestion from the Ambassadors that the gendarmerie should be withdrawn would have been very badly received unless at the same time the suggestion was made to the Japanese that their landing forces should be withdrawn, a solution which the Japanese, in the extremely serious situation which had now arisen, were not in the least likely to consider.
- 41. The Japanese had undoubtedly been caught in a dilemma. They had evacuated the whole of the Yangtze Valley, and many thousands of Japanese civilians had been concentrated in Shanghai as in a city of refuge. Anxious as they might be to keep hostilities away from Shanghai, their whole China policy and recent activities in North China had aroused passions which the sight of a Japanese uniform drove to the edge of madness. Though many solutions were discussed during the ensuing weeks, in fact the only alternatives before the Japanese were either to withdraw their armed forces from Shanghai completely

or else to strengthen them sufficiently to afford adequate protection to their nationals. Unwisely they chose the latter course, and from the moment when the naval reinforcements appeared on the scene all hope of keeping Shanghai out of the arena vanished.

- 42. It quickly became evident that the Chinese threat to take action in the event of reinforcements being landed was not a bluff. They immediately threw a barrage of sunken ships across the Yangtze at Kiangyin to prevent the Japanese fleet from entering the river, and another across the Whangpoo at the upper limit of the French Concession to prevent access to the Chinese city at Shanghai and the Lunghwa arsenal and aerodrome; and the 87th and 88th Divisions—considered to be among the best in the Chinese army—closed in and occupied the North Railway Station and Kiangwan. Hostilities commenced with sniping and desultory firing, appropriately enough on Friday, the 13th August. On the following day the Chinese launched a furious attack on the Japanese flagship Idzumo and the other Japanese craft in the river. The coup, if skilfully executed, might well have had a paralysing effect on the Japanese. Unfortunately, however, for the Chinese cause, the inexperienced Chinese pilots caused almost no injury to their naval objectives, while, on the other hand, they dropped bombs at two of the most crowded street corners in the International Settlement and French Concession, inflicting casualties which ran into four figures. These air attacks and the anti-aircraft action of the Japanese caused complete chaos. The whole of the water-front became practically untenantable; the banks closed their doors, and the British consulate-general, situated in a particularly dangerous spot, was hastily evacuated.
- 43. The avowed intention of the Chinese was to drive the Japanese forces out of Shanghai altogether before further reinforcements could be brought up, and simultaneously with the air action a heavy attack in overwhelming numbers was commenced on the Japanese positions all the way from the North Railway Station to the tip of the International Settlement at Yangtze-poo. The attack failed, and though it was renewed time after time in the ensuing days, the Japanese continued to hold intact, except for brief intervals, the whole of their original front. Though an offensive carried on through the streets of a city is considered to be one of the most expensive and difficult forms of warfare, nevertheless the Chinese, with the overwhelming forces at their command, should have been able to press it home, and their failure to do so afforded a fair indication of the immense disparity between the Chinese and Japanese military machines.
- 44. The hostilities spread round to the Pootung shore of the Whangpoo, and Nantao, on the further side of the French Concession, became a target for naval and air bombardment. As the scope of the hostilities spread, the position of the foreign communities became more precarious. There was already one British battalion in Shanghai. Immediately the gravity of the situation was realised Brigadier Telfer-Smollett asked for two more battalions. The first of these arrived from Hong Kong on the 17th August and the second on the 18th August. The French, Americans and Italians also brought in strong reinforcements.
- 45. As in 1932, the Japanese navy found that it had taken on more than it could manage, and the army had to come to the rescue. On the 23rd August the first portion of the Japanese Expeditionary Force reached Woosung, and covering forces, supported by warships, managed to establish themselves ashore, both at Woosung and at Liuho, further up the Yangtze. This was the beginning of the end. The Chinese held on tenaciously to the suburb of Chapei for two months longer, but gradually their left flank was turned, and on the 26th October they were forced to abandon this suburb, which went up in flames behind them. The effort to hold Chapei against the overwhelming weight of artillery and aircraft fire which the Japanese were able to concentrate against them was extremely wasteful both in men and material, and from this time onward the Chinese forces were never again in a position to make any effective stand. As long as possible they rested one flank on the foreign areas so as to prevent the severance of the important link between Shanghai and the rest of China, but this link was at length severed on the 9th November, when the Japanese completely surrounded Shanghai. The Chinese forces fell back on prepared positions further west, which it was confidently expected they would be able to hold for a considerable period; but demoralisation had set in. The new Chinese lines were almost immediately

turned. Wusih, Soochow, Chinkiang fell in quick succession, and on the 13th December the Japanese forces occupied Nanking. To round off their conquests in this area they occupied Wuhu on the west and Hangchow on the south

- 46. Meantime the Japanese forces in North China had been continuing their southward advance. Paoting, capital of Hopei, fell on the 24th September; Taiyuan, capital of Shansi, on the 9th November. The Japanese advance along the Tientsin-Pukow Railway brought them to the border of Shantung Province about the middle of October, and what they would do next was the subject of much speculation. Shantung was at this time the object of complicated political manœuvring between the Chinese and the Japanese. The Japanese were not only concerned for the safety of their valuable property at Tsingtao, but they had reason to believe that they would be able to seduce General Han Fu-chu, the chairman of the Provincial Government, from his allegiance to the Central Government, in which event they would be able to secure control of the whole province without fighting for it.
- 47. Han Fu-chu, however, whatever his personal inclinations may have been, was subject to Central Government influences, which he was either unwilling or unable to resist, so, although there were frequent reports that he was on the point of coming to terms with the Japanese, these eventually came to nothing. He was successful, however, in keeping the Japanese military command in a state of uncertainty, which restrained them for a considerable period from pressing their advance into the province. At length, however, apparently exasperated by the chairman's continued shilly-shallying, they resumed their southward advance, at the same time threatening a landing on the Shantung coast north of Tsingtao. On this, the Chinese destroyed first the Japanese property at Tsinan and Weihsien, and finally at Tsingtao. The last act of this drama was being played as the old year died: the Japanese mills dynamited, the Chinese officials and almost the whole of the Chinese population in flight, and the remnants of the foreign residents policing the town while awaiting the arrival of the Japanese forces.
- The Central Government had, at an early stage in the hostilities, envisaged the possibility that it might be compelled to evacuate Nanking, and had made preparations for this eventuality. In July a plan was formed to abolish temporarily the Ministries embraced in the Executive Yuan and to create a special Supreme War Council with departments assuming, but extending, the powers of the Ministries. In August this plan was abandoned, and the existing Military Affairs Commission was enlarged by the inclusion of departments with functions similar to and supplementing those of the Ministries. The departments in question dealt respectively with war operations, political affairs, heavy industries, economic affairs, publicity, people's training, commissariat and communications. They absorbed all that part of the work of the Ministries which had any relation to the conduct of the war, and the Ministries, though outwardly still functioning normally, were by so much reduced in importance. Finance, foreign affairs and education were in theory excluded from the scope of the Military Affairs Commission, but in practice all matters of importance, even those affecting these Ministries, were submitted to the final arbitrament of the generalissimo and his immediate advisers.
- 49. At the same time (mid-August) there was set up an "Advisory Council for National Defence" or War Senate of twenty-four members (subsequently increased to seventy-five), comprising representatives of all parties and influential organisations in the country, including the Communists and the National Salvation Association. In form, this was a concession to the ideology of the "united front," but, in fact, the generalissimo was virtual dictator.
- 50. As soon as hostilities broke out at Shanghai, Nanking became the objective of Japanese aerial attack. All valuable archives were accordingly removed to Hankow, Hong Kong and elsewhere, and Government offices, such as the Ministries of Foreign Affairs and Communications, which formed excellent targets from the air, were partially evacuated, their work being carried on in private houses scattered in different parts of the town, with a liberal supply of underground shelters, to which the staffs retreated at the sound of the air raid alarm. In these conditions the Government continued to function in Nanking with more or less efficiency, and stood steady even in the face of the threat of intensive air attack made by the Japanese Naval Commander-in-chief on the

19th September. The situation was, however, entirely changed by the advance of the Japanese land forces, and on the 20th November, when the Japanese were already at Soochow, an official statement was issued announcing that the seat of the National Government had that day been removed to Chungking. The evacuation of the Government had already commenced and was completed within a week. The President of the Government, with the headquarters of the National Government and the five Yuans, went to Chungking, and the various departments of the Government dispersed in different directions, some (including the Ministries for Foreign Affairs and Finance—by now reduced to mere skeletons) to Hankow, others to Changsha, Chungking and Hengyang. The generalissimo remained in Nanking with Mme. Chiang until the Japanese were close to the city. He then moved to Kiukiang, and thence, after a short interval, to Hankow, where the chief personalities of the Administration gradually assembled, and an appearance of government was resumed.

- 51. One of the most important and difficult problems with which the Japanese had to deal was the rebuilding of the civil administration in the areas occupied by their troops. The Chinese adopted as a deliberate policy the devastation of the areas from which they were compelled to withdraw. This policy of the scorched earth consisted in the destruction of bridges, harbour works, power plants, mills, railways, &c., in fact, of all the material things which might be turned to economic account by the invaders. It was carried out very unevenly hardly at all in the north, but much more effectively in Shanghai and the Yangtze Valley, where, accompanied as it was by the mass evacuation of the area of hostilities by the inhabitants, it immensely complicated the task of recreating a civil administration and establishing peace and order. It will be appreciated that where the Japanese were able to occupy an area without too much disturbance of the economic life of the inhabitants and without breaking up the civil administration completely, they took it over, so to speak, as a going concern, and all that they had to do was to substitute the necessary number of puppets at the top to ensure that the effective control rested in the hands of the Japanese army. Where, however, the economic life of the people was destroyed and with it the allimportant sources of revenue for the maintenance of a civil administration, and where, in addition, the local gentry refused to co-operate, the task of the Japanese became arduous in the extreme. So far as they could, the Japanese military authorities set up in each town as it was occupied a local Peace Preservation Association (or committee). It was in theory established in the interests of the local community by the spontaneous action of its leading members for the declared purpose of maintaining the currency circulation, preserving law and order and restoring communications and the transportation of food-stuffs. These associations played a prominent and important part in the subsequent political and constitutional development of the occupied areas.
- The Peking Local Peace Preservation Association, which was destined to play the major rôle in this connexion, was established on the 1st August under the chairmanship of General Chiang Chao-tsung (an aged retired pre-Republican official) and with a standing committee of nine, which included several members of the Hopei-Chahar Political Council, which body still remained in existence. Administrative control, however, soon passed into the hands of Pan Yu-kuei, a zealous and undisguised supporter of the Japanese cause. The announcement that the Hopei-Chahar Political Council had dissolved itself followed in due course on the 19th August, when the last vestiges of its control were transferred to the organisation which, in the meantime, had become restyled the "Peking Local Maintenance Association." A similar association had, meanwhile, been established at Tientsin, and others were being set up at Tatungfu, Paotingfu, Taiyuan and other large centres in the wake of the Japanese advance. It was generally recognised that once their primary function of dealing with the civil affairs of localities in the zone of actual military operations had been fulfilled they were likely to be superseded or absorbed by a more centralised form of government, and it seemed likely, in view of the past history of the question, that this would take the form of a Separatist Administration embracing the five provinces of Hopei, Chahar, Suiyuan, Shansi and Shantung, or a North China Autonomous Government on the model of the East Hopei Administration, which would be admitted to equal membership of a tripartite commonwealth with Japan

and Manchukuo. No kind of Government could, in any case, serve its purpose unless a sufficient number of suitable persons were prepared to take service under it—and it was essential, in order to maintain the façade of self-created government, that such persons should be Chinese of reasonable standing. It was obvious almost from the start, however, that the Japanese would find considerable difficulty in obtaining the necessary candidates, who could combine the qualifications of being respected by the Chinese population, on the one hand, and of being sufficiently amenable to Japanese direction on the other. Several persons were generally believed to have been unsuccessfully approached by the Japanese at one time or other with a view to accepting the headship of the new State, among whom the most prominent were Marshal Wu Pei-fu; the ex-Presidents of the Republic of China, Hsu Shih-chang and Tsao Kun; and the ex-tutor of the former Emperor of China, Hsuan Tung (now Emperor Kang Te of Manchukuo), Cheng Hsiao-hsu. The names of the Emperor Kang Te himself, and his kinsman Pu Wei, were also mentioned in connexion with the prospects of an imperial restoration, though the consensus of opinion regarded such an eventuality as unlikely, except as a last resource, particularly in view of the very qualified success of the corresponding experiment in Manchukuo.

- The anticipated constitutional change did not materialise for some time. It is probable that this crucial step had to be retarded owing to the complications arising out of the diversion of man-power and military material, resulting from the unexpected resistance encountered at Shanghai. Towards the end of October, however, as the Chinese opposition began to show signs of weakening, Japanese interest in the political side of their adventure revived. The Peking Maintenance Association, in conjunction with its Tientsin counterpart, formed a new joint organisation under the title of the Federation of Peking and Tientsin Local Maintenance Associations, while early in November there came into being a subsidiary unit of the Peking Association, called the Hopei Local Administrative Council, to deal with civil, financial and relief matters, not only in Peking, but in some nineteen districts in Hopei. It is reported that this council soon after its inception appointed ten magistrates, who duly proceeded to their respective posts, and that of these, four came back post-haste, one less a hand cut off by bandits, while the other six were never heard of again. Though without official confirmation, the story may well be true in view of the general disorganisation existing in the interior districts where the Chinese administration had broken down, and the effective authority of the Japanese was frequently limited to a few miles on either side of the railway lines.
- 54. There was now another lull for a month; the Japanese were clearly unwilling to take any irrevocable step in regard to the political situation so long as there remained any possibility of coming to terms with the Central Government, with whom certain exchanges were taking place as described in paragraphs 56 to 68 of this report. But these broke down, and upon the fall of Nanking on the 13th December a new régime was brought into being, under the name of the "Provisional Government of the Chinese Republic," claiming jurisdiction over the whole of China and with its headquarters temporarily at Peking, This was immediately followed by an announcement that the Joint Peking-Tientsin and the Peking Local Maintenance Associations were winding up their affairs, and that the East Hopei Anti-Communist Autonomous Government had expressed its readiness to be merged in the new Provisional Government. Incidentally, the East Hopei Autonomous Government undertook, as part of the arrangement, to pay an indemnity of 1,200,000 yen in compensation for the massacre of Japanese nationals at Tungchow at the end of July. The new régime took over the Chinese Maritime Customs at Tientsin and Chinwangtao on the 15th December.
- 55. The Commander-in-chief of the Japanese forces issued a statement pledging the army's support to the new Government, but the Japanese Government's official attitude had not been declared by the end of the year. It was confidently expected, however, that it would withdraw recognition from the Central Government, thus placing General Chiang Kai-shek in the position of a provincial war lord.

Peace Negotiations.

56. In the course of September conversations took place between unofficial Chinese and Japanese (but with the blessing of their respective officials), with a view to exploring possible bases for peace discussion. There were indications that the Japanese Government were much concerned at the way in which the situation was developing, and would at this stage gladly have acquiesced in peace terms which, while maintaining the original Hirota "Three-Point Policy," would not be punitive in character. His Majesty's Government indicated to the Japanese Government their willingness to further any effort for the restoration of peace, and on the 4th October His Majesty's Chargé d'Affaires, acting under instructions, communicated to General Chiang Kai-shek informally certain terms on which there were definite indications that the Japanese would be willing to make peace. These were as follows:—

(a) North China.

(1) Neutral zone to be established from which provincial and Central Government troops would be excluded. This zone to be policed by Peace Preservation Corps. Zone would extend to south of Peking and Tientsin. Japan would keep same number of troops as before to protect her nationals. Number would probably be about 5,000.

Number would probably be about 5,000.

(2) North China regime would be subject to Nanking, who would undertake that regime would not be unfriendly to Japan. "War lords" hostile

to Japan would be eliminated.

(3) Japan to obtain certain economic concessions, but no exclusive rights, and to respect interests of third parties whose co-operation, particularly that of Great Britain and the United States, she regarded as essential for economic development of China.

(4) Japan considered it the ambition of Inner Mongolia to obtain

independent status, and wished to assist her to achieve this ambition.

(b) Settlement of Outstanding Sino-Japanese Questions.

This meant particularly Manchurian question. De jure recognition was not insisted on, but China was to recognise the de facto existence of Manchukuo and undertake to abstain from creating difficuties for Japan in Manchukuo.

(c) Future Relations.

Japan wished an express undertaking that China would meet her half-way in any attempt to put Sino-Japanese relations on a new and friendly footing; in particular that Nanking would resist the spread of communism in China. Japan had no intention to interfere in China's internal affairs by virtue of any Chinese assurance to combat the spread of communism. Special arrangements were required in North China, without infringing Chinese sovereignty to ensure prevention of infiltration of communism. Japan would seek to negotiate for lowering of Chinese import tariff and for more normal development of air and railway communication.

- 57. The generalissimo's reaction was unfavourable. He remarked that Japan was evidently hoping to get all she wanted without further fighting, but that China would go on until she had complete sovereign and administrative rights in North China.
- 58. Meantime, China had appealed to the League of Nations, and on the 8th October the Assembly adopted the findings of the Advisory Committee (1) affirming Japan's contravention of her obligations under the Nine-Power Treaty and the Paris Pact, and (2) recommending that those members of the League who were parties to the Nine-Power Treaty should be invited to initiate the consultation provided for in that treaty as soon as possible, associating with them in their work other States having a special interest in the Far East. On being invited to attend the conference, which was convened at Brussels in consequence of this resolution of the League, however, the Japanese Government refused, on the ground that Japan's action in China constituted self-defence in face of China's anti-Japanese policy and provocative acts of force. In a statement accompanying their formal reply, they reiterated their view that Sino-Japanese difficulties could be solved only by direct negotiation between the two parties, and

that if the Powers wished to co-operate in a settlement of the conflict they should "understand the true intentions of Japan and take suitable steps to make the Nanking Government reconsider their attitude and policy."

- 59. There was, however, little prospect of the Chinese agreeing to enter into direct discussions with the Japanese. Their attitude throughout was that any arrangement with Japan must be based on the League of Nations and/or the treaty of the 6th February, 1922, relating to principles and policies to be followed in matters concerning China (the so-called Nine-Power Pact), since it was essential for China that any such arrangement be effectively guaranteed by the Powers.
- 60. The next move came from Germany. According to information given by the Japanese Vice-Minister for Foreign Affairs to His Majesty's Ambassador in Tokyo, the German Ambassador sometime in mid-November sounded the Minister for Foreign Affairs on the desirability of mediation by the German Government, and about the same time the German Ambassador in Nanking was making similar soundings among the Chinese leaders, only to discover that the Chinese terms—particularly a stipulation for the withdrawal of all Japanese troops as a condition precedent to an armistice—afforded no basis for further negotiations. Thereupon the German Ambassador in Tokyo informed the Minister for Foreign Affairs that at that time there did not seem to be any opening for German mediation.
- 61. There were many rumours regarding Italian mediation, but no action seems to have been taken by the Italians.
- 62. A few days later one of the German military advisers in Nanking stated that General von Falkenhausen (chief adviser), had informed the German Ambassador that in his opinion the moment was opportune for the Powers to bring pressure to bear on China to make peace, since the Chinese leaders could now accept the Powers' advice without loss of face, and he thought they, including General Chiang Kai-shek and General Pai Chung-hsi, would be glad to do so.
- 63. The Japanese seemed to be of the same mind as General von Falkenhausen, and confidently to expect that now that the Chinese armies had been thoroughly well beaten in Shanghai the Government would be ready to talk peace. The Minister for Foreign Affairs informed the American Ambassador that, if peace were made at that stage, the Japanese terms would be reasonable and China would not be required to surrender one foot of territory, but if the campaign continued Japan's terms would become increasingly rigorous.
- 64. Possibly as a result of General von Falkenhausen's recommendation a further *démarche* was made by the German Ambassador in China, who at the beginning of December communicated to General Chiang Kai-shek the following proposals for a peace settlement:—
 - (1) Creation of an Inner Mongolian State under Japanese domination.
 - (2) Demilitarisation of almost the whole of the six northern provinces of China, which were to be administered by Chinese approved by the Japanese.
 - (3) Creation of a neutral zone round Shanghai.(4) China to accede to the Anti-Comintern Pact.
 - (5) Sino-Japanese Trade Agreement giving special privileges to Japan in the China market.
- 65. It is open to doubt whether these proposals were made by the German Ambassador with the express authority of the Japanese Government. The Vice-Minister for Foreign Affairs in Tokyo informed Sir Robert Craigie that the démarche had been made without the knowledge of the Japanese Government, though the proposals were the expression of Mr. Hirota's earlier ideas on the subject. The generalissimo is reported to have informed the German Ambassador that he accepted the terms as a basis for discussion, but could not agree to any terms which infringed China's territorial and administrative integrity; and he further asked the German Ambassador to continue as a medium for German mediation.

- 66. With the fall of Nanking and developments in Peking, however, the Japanese attitude stiffened. On the 26th December the German Ambassador handed Dr. H. H. Kung a memorandum containing the following, described as Japan's "basic conditions for peace":—
 - (1) China to abandon her pro-Communist and anti-Japanese and anti-Manchukuo policy and sincerely to co-operate with Japan and Manchukuo in the exercise of an anti-Communist policy.

(2) Demilitarised zones and "special régimes" to be established in "necessary areas."

(3) China to conclude with Japan agreements for close economic co-operation of China with Japan and Manchukuo.

(4) China to make the "necessary indemnification."

- 67. The German Ambassador stated that these terms had been received by his Government from the Japanese Government with a request that they should be passed on to the Chinese Government and an intimation that previous terms presented by him were to be considered cancelled in view of the changing military situation.
- 68. No reply had been given to these proposals by the end of the year, but the indications were that a negative reply would be given. Acceptance would, indeed, have meant virtual vassalage to Japan, the terms by their wide scope and vagueness being capable of almost any interpretation the Japanese cared to place on them

MONGOLIA.

- The situation in Mongolia remained generally quiet during the first half of the year. Developments resulting from the Sino-Japanese incident at Lukouchiao, however, brought Mongolian affairs again into the limelight. As hostilities extended to the region of the Great Wall, the Japanese despatched an expeditionary force, largely composed of units of the Manchukuo army, with Mongol auxiliaries, to protect the rear of their forces operating in North China from attack by the Chinese armies from Suiyuan and Chahar. After assisting in the defeat of the Chinese defenders of the Nankou Pass, the expeditionary forces proceeded westwards, and eventually reached Paoton in October, having taken Kalgan, Pailingmiao, Suiyuan and Kueihuacheng in their stride without undue opposition. The Japanese thereupon, pursuing their traditional tactics of alienating the Mongols from association with the Chinese Government, succeeded, with the assistance of the Manchukuo army commander, General Li Shou-hsin, in bringing into being on the 28th October the so-called Inner Mongolian Autonomous Government. This Government, the formation of which was preceded by a meeting of delegates claiming to represent 5 million inhabitants of Inner Mongolia, purported to be the spontaneous creation of the Mongols. Its capital was to be at Kueihua, renamed Houho (or Hohogoto), with jurisdiction limited in the first instance to the four Leagues of Chahar and Suiyuan. The septuagenarian Prince Yun of the Ulanchab League was appointed chairman, and Teh Wang, of the Silingol League, vice-chairman, while Li Shou-hsin was nominated as Minister of War. As a sentimental appeal to old Mongol traditions, a yearly notation was adopted based upon the reign of Genghiz Khan, the year of the foundation of the Government being accordingly recorded as the 732nd year of Genghiz Khan.
- 70. The aims of this Government, as publicly declared by Prince Teh, doubtless after careful coaching by the Japanese, was the eradication of communism, universal education, industrial development, and closer affiliation with the Japanese. The conclusion of the Sino-Soviet Pact of Non-Aggression, signed at Nanking on the 21st August, had already been viewed with apprehension by the Japanese, whose suspicions of the existence of secret clauses designed to manœuvre the Outer Mongolians into taking the offensive against Japan found expression in various Domei and other press articles. The main motive of the Japanese in sponsoring this autonomous administration would therefore appear to have been the creation of a buffer State between Soviet influences in Outer Mongolia and China proper.
- 71. This anti-Communist front was subsequently strengthened, at least in theory, by the formation at Kalgan on the 22nd November of a "Mongolian Frontier Joint Commission" (Meng Chiang Lien Ho Wei Yuan Hui), of which

the constituents were the same Inner Mongolian Autonomous Government, and the two "Autonomous Governments" of Southern Chahar and Northern Shansi, which likewise owed their creation to the Japanese invaders. No effort was made to disguise Japanese participation in this particular venture as the relevant agreement, in addition to providing for a Japanese high adviser and several other Japanese counsellors to the commission, expressly stated that, though drawn up in the Chinese, Mongolian and Japanese languages, the Japanese interpretation was to be authoritative.

- 72. The first act of this commission was to promulgate regulations for the organisation of a Meng Chiang (Mongolian Frontier) Bank, with a nominal capital of 12 million dollars to be equally contributed by the three constituent members of the commission. According to reports emanating from Japanese sources, the bank was to absorb the South Chahar and Fengyeh Banks, and the Suiyuan mint, and to inaugurate its head office at Kalgan on the 1st December. Pending the issue of its own notes, existing currency was to continue in circulation. Owing to the difficulty of obtaining reliable first-hand information of events in territory under Japanese occupation, details regarding the purposes and operations of this bank are of necessity based on Japanese-inspired press reports. It is likely, however, that the bank is primarily intended as an agent for the circulation of Japanese currency in Mongolia, as well as for financing Japanese purchases of wool direct from the producing areas in the manner most profitable to themselves.
- 73. By the end of the year the Japanese had further consolidated their material position by taking over the Postal Administration in Inner Mongolia, and had begun making plans for controlling and extending telegraph and telephone services north of the Wall under a unified organisation which would eventually take over postal communications as well.
- 74. At the same time the Japanese have been at pains to win over the sympathies of the mistrustful Mongols by exploiting their religious susceptibilities through the medium of various prominent members of the Buddhistic hierarchy. In this cause the Anchin Lama, judging by various public statements made by him, particularly during the course of a visit to Manchuria (doubtless at the invitation of the Japanese) in November, has proved himself an amenable and vigorous propagandist.
- 75. News from Outer Mongolia is increasingly scarce, but its position must inevitably render it the focus of political intrigue, with Japanese emissaries bent on extending the anti-Communist buffer State to the utmost, and the Union of Soviet Socialist Republics compelled by force of circumstances to retain and even strengthen her domination of the strategic border territory.

Sinkiang.

- 76. At the beginning of the year the Provincial Government was in nominal control of the whole of Sinkiang, but in the south its authority was precarious. The garrison at Khotan was Tungan, and the Military Governor of Kashgar was Mahmud Shih Chang, who, in spite of professions of loyalty to Urumchi, clearly did not find the increase of Soviet influence in the Government to his taste. It came, however, as a complete surprise to the authorities when, on the 2nd April, he fled from Kashgar to Yarkand and thence to India, where he spent the rest of the year ostensibly waiting for instructions from Nanking. No instructions came, however, and in December he announced his intention of going on to Haj.
- 77. His flight from Kashgar was a great blow to the Moslem population, for, since the suppression of the last Tungan rebellion, the Provincial Government had been attempting to introduce reforms which, inspired by Soviet ideology and administered by a hated chief of police, Qadir Haji, would have been unpopular even had they not encroached on religious freedom. With Mahmud in charge, these reforms could not be too rigidly enforced, and his flight inevitably caused much apprehension among Tungans and Turkis.
- 78. It was, therefore, a matter for no great surprise when on the 20th May a rebellion broke out in the south of the province. A force of 1,500 men, partly Tungans and partly former Turki troops of Mahmud's, advanced on Kashgar Old City from the east, and captured it after ten days' fighting, during which His

Majesty's consulate-general was in some danger from stray bullets. Ma Hu-shan, the leader of this force, announced that he was acting in the interests of the Provincial Government, but the Chinese garrison of the New City did not believe this improbable claim; they resisted his siege, and were reported to have massacred all the Turkis in the New City. On the other hand, the Tungans, learning from their last insurrection, attempted at first, and with success, to win the sympathy of the population, and there was very little looting after the capture of the Old City. Later, however, economic stress compelled them to exact heavy taxes in money and kind, and the townsfolk profited little by the change of control.

- 79. June and July saw considerable fighting in the south of the province. After taking Kashgar the Tungan-Turki forces moved east and captured Maralbashi, the strategic key to South-West Sinkiang, and then turned north towards Aksu. At this point they held practically all Southern Sinkiang except Kashgar New City, and it appeared that they might well overrun the whole province. Local feeling was still favourable to them, and in the 36th Tungan Division they had the largest armed force in Sinkiang, so that there was no reason to suppose that the provincial troops would offer them any very serious resistance.
- 80. In September, however, the rebellion suddenly collapsed. The prime cause was the mutiny of the 2nd Tungan Brigade under Ma Sheng-kuei, whom the Provincial Government had presumably been able to bribe. As a result Maralbashi was lost, and with it inevitably control of the southern oases. The Tungans under Ma Hu-shan abandoned the siege of Kashgar New City, which they had been conducting in a desultory fashion since the beginning of June, and provincial troops regained both cities. Ma himself, after plundering the Yarkand district, fled to India, as Mahmud had done; and, in spite of the request of the Sinkiang authorities for his extradition, he too was given asylum.
- 81. The immediate result of this sudden change in the situation was naturally an outbreak of banditry in the area that had been first controlled and then pillaged by the Tungans, an outbreak that is unlikely to be suppressed until the Provincial Government can spare troops in far larger numbers than are at present available. The Government has, however, already reasserted its authority as far south as Khotan, and it appears that the Tungans will not again, for a long time at least, constitute a serious political danger. For the first time in its history the present Provincial Government can exercise effective jurisdiction over the south-west of the province.
- 82. Kashgar itself escaped the depredations of bandits, but was subjected instead to the vindictiveness of the chief of police, Qadir Haji, who took revenge for his rough treatment during the Tungan control of the city by drastic punishment of any he suspected of having helped the rebels. A particularly unpleasant case occurred at the end of November, when a British Indian was found murdered within a few hundred yards of the British consulate-general. At Qadir Haji's request, another British Indian was sent to him for questioning, and it was subsequently given out that this second man had fled after confessing to the crime. His Majesty's consul-general was unable to believe this story, and was convinced that the police were implicated in the first murder and had endeavoured to conceal their guilt by committing a second.
- 83. This was but one of a number of cases in which His Majesty's consulgeneral was dissatisfied by the attitude of the authorities. Except during the period of Tungan control, the officials, local and provincial, were consistently obstructive, and it was clearly their policy, as in the past, to hamper British traders in every way possible. Even consular messengers with special passports were detained for long periods. It was, unfortunately, impossible to take up any of these cases directly with the chairman of the Provincial Government, for Sir Eric Teichman's recommendation that a consulate should be opened at Urumchi has not yet been acted on, and, though both His Majesty's consul-general and His Majesty's consul travelled considerably during the year, neither of them was able to pay the capital a visit. However, though personal contact might prevent aggravation of certain incidental difficulties, there is no reason to suppose that it would be likely to overcome the set policy of the provincial officials, dictated and backed as it is by powerful Soviet interests.

Tibet.

- 84. The fear that the Chinese attempt to extend their authority in Eastern Sikang might bring them into conflict with Tibet proved groundless, as Marshal Liu Wen-hui was careful to employ conciliatory methods, and the presence of his troops was welcomed by the inhabitants as a safeguard against the return of the Communists, who had ravaged the country in the autumn of 1936. In consideration of the distress caused by their depredations Marshal Liu remitted for a year certain taxes and the ula (a sort of corvée). He also established some schools and made preparations for laying telegraph lines. As a part of his administrative reforms Sikang was divided into thirty-three "districts," of which the fifteen to the west of the Kinsha (the Upper Yangtze) were left under Tibetan control, while nominees of Liu's were appointed to the other eighteen.
- 85. In spite of these reforms a disorganised rebellion broke out in the summer, and there was some sporadic fighting in the south of the province. The cause of the rebellion appears to have been in part the fact that, in search of revenue to pay for his reforms, Marshal Liu had increased the taxes on goods in transit (particularly on the Tachienlu–Lhassa road) to an extent that more than offset the direct taxes he had remitted; and in part it was no doubt due to political dissatisfaction with an alien ruler. There has been no recent news of this rebellion, which may be assumed not to have reached very serious proportions.
- 86. It was reported in the summer that a new incarnation of the Dalai Lama, who died in 1933, had been found; but this was not confirmed, and the Government at Lhassa remains in the hands of the Regent and Council.
- 87. The Panchan (Tashi) Lama, the question of whose return to Tibet had hung in the balance throughout 1936, died in November 1937. He had spent the winter at Yushu (Jyekundo), but showed signs in the spring of a serious intention to resume his journey. The chief obstacle was still the objection of the Tibetan Government to his being accompanied by a Chinese military escort; this objection was so strong that Tibetan troops actually took up positions on the frontier, presumably in order to resist the escort by force. His Majesty's Ambassador made repeated informal representations to the Waichiaopu that it was undesirable for the Chinese Government to press the point in face of such clear indications of the Tibetan Government's views; but these representations were not favourably received, and it was through other channels that a compromise was arranged, whereby the escort should accompany the Panchan Lama to Shigatse direct, instead of via Lhassa, and should immediately return to China by sea. Thereupon the Panchan Lama despatched much of his luggage in advance and himself moved as far as Lungshogun. However, instead of continuing to Tibet he appears to have changed his mind for the last time, as he returned to a monastery in Kanze, where he was taken ill early in November; and there, on the 30th, he died.

Military Operations.

- 88. The outbreak of Sino-Japanese hostilities on the 7th July transcends by far all other military events during the year 1937. This event indicated the resumption by the Japanese in full force of the imperialist forward thrust on the Asiatic mainland, which began with the seizure of Manchuria in 1931.
- 89. It will, however, be necessary to give a brief résumé of the military activities during the first half of the year.
- 90. The closing weeks of 1936 found the military situation in China as follows:—
 - (a) The main Chinese Communist forces under Chu Teh, Mao Tze-tung, Hsu Hsiang-chien, Hsiao Ko, Ho Lung and Hsu Hai-tung had, as the result of constant harrying during the course of the year by Central Government forces, been driven into North-West and North-East Kansu.

- (b) In Suiyuan the Chinese forces had succeeded in taking Sharamuren on the 11th December, 1936, and were threatening an attack on Shangtu and Chapsor, two important towns just within the western boundary of Chapar
- (c) In Shensi the Central Government were endeavouring to bring about a settlement of the "Sian incident" which had led to the detention in Sian of General Chiang Kai-shek by Generals Yang Hu-cheng, chairman of Shensi Province, and Chang Hsueh-liang, Commander of the old North-Eastern Army.
- 91. In order to follow the course of events up till the outbreak of Sino-Japanese hostilities it will avoid confusion if the activities of the Chinese Communists and Shensi rebels are bracketed together.
- 92. It was generally expected that the release of General Chiang Kai-shek and his return to Nanking on the 25th December, 1936, would bring about an early settlement of the Sian incident. However, the failure of the Central Government to allow Chang Hsueh-liang to return to Sian, and his subsequent trial and punishment by a military tribunal caused very justifiable misgivings to arise in the minds of Yang Hu-cheng and Chang Hsueh-liang's subordinate commanders. This in turn drew them much closer towards the blandishments of the leading Chinese Communists, such as Chu Teh and Mao Tze-tung.
- 93. By the middle of January Central Government troops were again advancing westwards along the Lung-Hai Railway with Sian as their objective, whilst indisputable proof was forthcoming that the Communist forces had moved south-eastwards from their stamping grounds in Kansu and were concentrated to the north and north-west of Sian.
- 94. In addition "Red" emissaries, including Chow En-lai, chief political agent of the Communist forces, were seen walking openly about the streets of Sian.
- 95. The evacuation of practically all foreigners from Sian and the vicinity, including some thirty British nationals, now became necessary. This was successfully accomplished between the 18th and 22nd January. This evacuation was not caused through any fear of anti-foreign actions on the part of the Communists, but it was felt that, should fighting eventuate, foreigners would be exposed to aerial attacks, the ordinary dangers associated with land operations and, what was more important, the prospect of looting by disorganised soldiery before the arrival at Sian of the Central Government forces.
- 96. In the meantime General Ku Chu-tung, chairman of Kweichow, had been appointed director of the Sian Provisional Headquarters of the Military Affairs Commission. He established his headquarters at Loyang in Honan, and by the 23th February he moved to his advanced headquarters at Tungkwan (Shensi-Shansi-Honan border) on the Lung-Hai Railway. At this time considerable activity was also being displayed by the Chinese air force based on Loyang.
- 97. There is little doubt but that, had political manœuvrings failed, Ku Chu-tung with the means at his disposal would have been able to deal successfully with the rebels. The latter possessed no air force and, generally speaking, no modern armaments. However, had serious fighting ensued, this would inevitably have led to the rebels being thrown into the arms of the Chinese Communists.
- 98. The situation was dealt with in accordance with Chinese characteristics, and without any fighting except minor skirmishes between partisans of both sides. Negotiations became the order of the day, and the Central Government, by threats, bribes, cajolery, promises and compromises, succeeded in preventing a definite alliance between Communists and rebels. This enabled troops under the command of Ku Chu-tung to occupy Sian without opposition early in February. Ku Chu-tung followed and established his headquarters at Sian about the 8th February. This concluded what might be described as a bloodless campaign, for it is doubtful whether either side, during the course of operations, suffered more that fifty casualties.

99. By the middle of April, when the final ripples on the political pond had subsided, the situation was as follows:—

(1) The Central Government, through the agency of Ku Chu-tung, had established a firm control over south Shensi, including the important Lung-Hai Railway.

(2) Yang Hu-cheng's rebellious army had been partly disbanded and partly assimilated within the ranks of units loyal to the Central Government. Yang himself had been persuaded to proceed on a tour of Europe and America.

(3) Chang Hsueh-liang had been severely dealt with, so much so that at the

present time it is doubtful whether he is still alive.

The old North-Eastern Army units had been transferred from Shensi and Kansu to other localities in Honan, Anhwei and Kiangsu,

where they were to receive badly needed reorganisation.

(4) The Chinese Communists had been compelled to withdraw to the central and northern parts of Shensi Province. In addition, it is quite certain that an arrangement had been arrived at by which the Communists were to be left in peace provided they on their part remained quiescent. This point was important, because it implied that, for the first time since 1927, the Communist leaders and the Central Government had, in the face of the possibility of Japanese aggression, come to an understanding.

(5) The Central Government, from a military point of view, had considerably strengthened its hand but, unfortunately, from many aspects, at the expense of Chiang Kai-shek. This was not distasteful from their point of view, but it had the serious effect of weakening Chiang Kai-shek's control over many of the most powerful and important

military members of the anti-Japanese clique.

100. And so ended a typical military-cum-political Chinese "incident," that demonstrated clearly the risks to which even the highest in the land were exposed when they pursued a policy of moderation in respect of Sino-Japanese relations.

- 101. The stage had been set for the now inevitable military clash between Chinese and Japanese interests.
- 102. The Sian incident brought to an end all Chinese hopes of further penetration eastwards from Suiyuan Province. The Chinese forces under General Fu Tso-yi contented themselves with their recent victories at Pailingmiao and Sharamuren over the Japanese-backed Mongolian-Manchukuo irregulars. In fact, all attention in this part of China was focussed on the Central Government's efforts to bring about a solution of what appeared to be a major crisis in Shensi, and, later, on the intransigent attitude being adopted by several of General Sung Che-yuan's (chairman of Hopei and commander of the XXIXth Route Army) subordinates regarding Japanese intentions in North China. Sung Che-yuan had been suspect from the time of his appointment, at the instigation of the Japanese, as chairman of Hopei, and the rising tide of anti-Japanese sentiment that was now being evinced throughout the whole of China, together with the possibility (and hope) that Sung Che-yuan would be the first to bear the brunt of Japan's wrath, brought about a "go-slow" policy in Suiyuan until the outbreak of Sino-Japanese hostilities. The Japanese, on their part, being sure of the bag, were content for the time being to let matters slide.
- 103. Sino-Japanese hostilities broke out at Liukouchiao in North China on the 7th July, 1937.
- 104. Space forbids a detailed account of the course of operations during the ensuing six months. This report will be restricted to a very general picture of what occurred.
- 105. On the outbreak of hostilities there were no modern Central Government troops in Hopei Province. To oppose Japanese aggression in the Tientsin–Peiping area there were three infantry divisions, one independent infantry brigade and two cavalry brigades of Sung Che-yuan's XXIXth Army, whose total strength amounted to about 60,000 men.

106. The nearest troops at close call were Wan Fu-lin's LIIIrd Army and Shang Chen's XXXIInd Army, located on the Kin-Han Railway at Paotingfu and to the south. Sung Che-yuan, in addition to being chairman of Hopei, was senior military commander. None of these troops possessed anything more than a negligible military value. Arms and equipment, particularly the artillery, were old and out of date. They had little defence against air attacks and no aeroplanes.

107. The Japanese, on their side, had some 550 men stationed at Fengtai, about 450 men of the Embassy Guard at Peiping, and a small detachment at Tungchow, some 18 miles to the east of Peiping. Troops at close call consisted of the Japanese garrison at Tientsin and troops that might be withdrawn from units stationed along the Pei–Ning Railway between Tientsin and Shanhaikuan.

Japanese aeroplanes began to arrive at Tientsin on the 11th July.

108. On the outbreak of hostilities Lieutenant-General Kamchiro Tashiro was senior Japanese military commander, with headquarters at Tientsin. He died in July 1937, and in due course was replaced by General Count Hisaichi Terauchi, who automatically became commander of the Japanese North China Expeditionary Force.

109. The inevitable happened, and after three weeks of indecisive negotiations and abortive compromises, interspersed with fresh incidents, the Japanese, with the aid of unrestricted aerial supremacy and modern equipment, had succeeded, by the end of July, in driving the Chinese forces, with very heavy loses, from the Tientsin-Peiping area. For details of what transpired on the night of the 7th July, and subsequent events leading to the occupation by the Japanese of Tientsin and Peiping, please see paragraphs numbers 19 to 23 of this report.

110. With the arrival of large reinforcements from Manchuria and by sea from Japan, the Japanese were now able to turn their minds of serious business.

- 111. Leaving the defeated Chinese forces to lick their wounds on the line Liuliho (Kin–Han Railway)–Machang (Tsin–Pu Railway), the Japanese forces moved north-westwards from Peiping, and by the 2nd August had forced the important Nankou Pass on the Peiping–Suiyuan Railway. With the aid of a mechanised brigade of Kwantung troops and Mongol irregulars Kalgan, the capital of Chahar, was occupied on the 25th August. The Chinese forces, consisting of one division of Sung Che-yuan's XXIXth Army and three divisions of Central Government troops under Tang En-po, retired in disorder south-westwards into Shansi Province.
- 112. To remove the Peiping-Suiyuan Railway out of the picture, it may be added that Kweihua, the capital of Suiyuan, was occupied by the Japanese on the 14th October and Paotou, the railhead, on the 17th October. The Chinese forces, under the command of Fu Tso-yi, chairman of Suiyuan, put up little opposition, and eventually withdrew southwards into Shansi.
- 113. The fighting in this area resulted in the Japanese gaining full control of the Peiping–Suiyuan Railway, and thereby driving a strategical wedge between Inner Mongolia and China proper. It also brought them within striking distance of China's vital communications through Kansu and Sinkiang to the U.S.S.R.
- 114. For the purposes of clarification, subsequent Japanese military operations in North China may be divided into three phases:—
 - (a) The drive southwards from Tatung (North Shansi) along the Tatung— Puchow Railway, combined with a drive westwards along the Cheng— Tai Railway from Shihchiachuang (West Central Hopei) on Tai yuanfu, the capital of Shansi.
 - (b) The drive south-westwards from Peiping along the Kin-Han Railway.
 (c) The drive south-eastwards and then southwards along the Tsin-Pu Railway. In this case the Japanese forces, having successfully occupied Tsinanfu, the capital of Shantung, advanced eastwards along the Kiao-Chi Railway, on Tsingtao, the important port on the Shantung coast.
- 115. As regards (a). With Kalgan, the capital of Chahar, in their hands, the way was now open for an advance through Central Shansi on Taiyuanfu, the capital. The first step was the occupation of Tatung, an important town in

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North Shansi, that guarded the back-door into the province. This was successfully accomplished on the 14th September. The Chinese forces (68th Shansi Division) put up such a poor show that the Divisional Commander, Li Fu-ying, was subsequently executed for incompetence.

- 116. The next step was the forcing of the Yenmen Pass, a place of great strategical importance, some 65 miles south of Tatung, and located in the mountainous region adjacent to the Inner Great Wall. The possession of this pass gave access to the Central Shansi Plain and the first objective of importance—Taiyuanfu.
- 117. In addition to the Central Government and provincial troops that had been forced to withdraw into Shansi from the Peiping—Suiyuan Railway area, the Japanese were now opposed by Shansi provincial troops (XXXIIIrd and XXXIVth Armies), and the Chinese Communists who had been organised into the VIIIth Route Army, under the supreme command of Chu Teh, who had been appointed a general in the Chinese forces for the occasion.
- 118. Yen Hsi-shan, the doddering chairman of Shansi, was nominally in command of the Chinese forces in Shansi.
- 119. The month of October saw some of the fiercest fighting that took place in North China during the half-year under reference. In addition to driving southwards from Tatung, a Japanese column advanced south-westwards from South-West Chahar and encountered heavy resistance in the area Kwangling-Hunyuan (North-East Shansi). However, the Japanese eventually broke down all opposition, and by the 1st October the Yenmen Pass was in their possession, and Taichow, Kuohsien and Ningwu (all south of the Inner Great Wall) had fallen into their hands.
- 120. In the meantime the Japanese had advanced rapidly southwards along the Kin–Han Railway, and their occupation, on the 11th October, of Shihchiachuang, an important railway junction on the Kin–Han–Chen-Tai Railways, enabled them to despatch a column westwards along the Cheng-Tai Railway with a view to co-operating with the Japanese forces advancing on Taiyuanfu from the north of Shansi.
- 121. Slight opposition was offered by the Chinese forces at the Niangtzekwan Pass on the Hopei-Shansi border, but by the 27th October the Japanese had broken through and were threatening Taiyuanfu from the east.
- 122. The Central Government made a belated effort to save Taiyuanfu by the despatch into Shansi of Government troops under Wei Li-huang, commander of the XIVth Army. However, this proved of no avail, and the Japanese were successful in occupying Taiyuanfu on the 9th November.
- 123. The Japanese now had to call a halt to their march southwards towards the Yellow River (Puchow), for purposes of reorganisation and strengthening their lines of communication, which by this time were being severely harassed from the west by units of the VIIIth Route Army (ex-Communist).
- 124. At the end of December they were holding a line running (approximately) from Siyang (25 miles south-west of Niangtzekwan), Taiku-Kiehsui (both on the railway south of Taiyuanfu), Fenyang (ex) (60 miles south-west of Taiyuanfu). In addition, they were maintaining a precarious hold over their lengthy lines of communication running from Tatung in the north to Taiyuanfu, and Shihchiachuang in the east to Taiyuanfu.
- 125. Turning to (b). With their attention fully occupied in the north-west, the Japanese were content to let matters remain quiescent on the Kin-Han Railway until the early part of September, when they succeeded in dislodging the Chinese forces from Chochow (35 miles south-west of Peiping). Following up their success they occupied Paotingfu, the capital of Hopei Province, on the 24th September and Shihchiachuang, further south, on the 11th October. The occupation of the latter place enabled them to despatch a column westwards along the Cheng-Tai Railway with Taiyuanfu as their objective.
- 126. The Chinese forces defending the Kin-Han Railway were in a complete state of disorganisation. Changes of command were frequent, and co-operation was conspicuous by its absence. Liu Shih, Pacification Commissioner for

Honan and Anhwei, who was in chief command, was eventually dismissed and his place taken by Cheng Chien, Chief of the Staff, who was sent up from Nanking. By the end of December no less than twenty-six Chinese divisions had been reported along the Kin–Han Railway and the area to the west of the Grand Canal. These troops had been drawn from all over China and what with language difficulties, personal animosities between the leaders and lack of combined training, they appeared to do everything but fight.

- 127. Continuing their march southwards the Japanese crossed the Hopei-Honan border and by the end of December had reached the line (approximately) Tsingfeng (South Hopei)-Anyang (North-East Honan).
- 128. As regards (c). On the Tsin-Pu Railway the Japanese plans were of a different character. Political considerations came into the picture. In order to avoid the destruction of valuable Japanese property at Tsingtao and Tsinanfu, they hoped to avoid fighting for Shantung. To obtain success it was necessary to persuade Han Fu-chu, chairman of Shantung, and concurrently commander of the IIIrd Route Army, to throw in his lot with them.
- 129. Han Fu-chu had been suspected of pro-Japanese sympathies for some years past, and in consequence the Central Government took what proved to be adequate steps to ensure that Han's movements were watched closely. In the first place, some of his subordinates were brought over under the cloak of patriotism. Yu Hsueh-chung's L1st Army was sent to the north-eastern part of the province, and finally Kwangsi divisions were despatched to the south part of the province. Han, who had proved one of the most capable administrators that had ever ruled Shantung, and far superior to many other incapable and traitorous provincial Governors, eventually fell between two stools. He gave up the unequal contest, was arrested, and duly executed for treason. Han's inability or disinclination to join forces with the Japanese brought the latter to Tsinanfu.
- 130. The Japanese forces in the vicinity of Machang were on the move again towards the middle of September. They advanced in the face of feeble opposition to the borders of Hopei and Shantung, and, after satisfying themselves that Han Fu-chu represented a lost cause, they crossed the border and occupied Tehchow (Tsin-Pu Railway) on the 4th October. Still cherishing a pious hope that their valuable property in Shantung might be saved, the Japanese moved cautiously southwards towards the Yellow River. By the middle of December they had come to the realisation that their hopes were to be dashed to the ground. They therefore crossed the Yellow River and occupied Tsinanfu on the 27th December. From Tsinanfu the Japanese commenced a movement eastwards along the Kiao-Chi Railway towards Tsingtao, and by the end of the year had reached Yitu.
- 131. The Chinese forces withdrew southwards, and as a parting gesture destroyed all the Japanese mills at Tsingtao, Weihsien and Tsinanfu. Only time will elucidate who was in actual command of the Chinese forces on this front. In the beginning Han Fu-chu appeared to be in supreme command. In November Feng Yu-hsiang, the Christian general, was sent from Nanking with a view to encouraging his former subordinates, Han Fu-chu and Pang Ping-hsun, Commander of the XLth Army. He was followed by Pai Chung-hsi, the famous warrior from Kwangsi, and at the end of the year Li Tsung-jen, Commander of the Vth Route Army (Kwangsi), was in charge of operations with headquarters at Hsuchowfu (North-West Kiangsu).
- 132. In the Shanghai area Sino-Japanese hostilities were precipitated by the murder, on Monument Road on the 9th August, of a Japanese naval lieutenant and his chauffeur. There is no doubt but that the Chinese were responsible for the murders, and it is equally certain that the Chinese military authorities were determined, as a result of the serious turn that affairs had taken in North China, to create a diversion and at the same time compel the Japanese to fight in an area that had been specially selected and secretly prepared for defensive warfare. The Central Government's best divisions (including the crack 36th, 87th and 88th Divisions) had been collected in the Shanghai–Hangchow–Nanking triangle, and, what was more important, the area was easily accessible

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to the important air bases at Nanking, Hangchow in Chekiang, and Nanchang in Kiangsi. Finally, by fighting with their right flank hooked on to the International Settlement, there was always the possibility of creating serious international complications. However, had the Chinese suspected that fighting in the vicinity of Shanghai would lead to the loss of Nanking, it is extremely doubtful whether they would have started the conflict. They thought, as did most foreign observers, that, if it came to the worst, the Japanese would content themselves with driving their forces away from the settlement. The Japanese, on their part, were faced with the alternative of either fighting or withdrawing their nationals from Shanghai. They chose the former.

- 133. For details of events leading up to the murders, and the subsequent arrival of the Japanese Central China Expeditionary Force under the supreme command of General Iwane Matsui, please see paragraphs 31 to 45 of this report.
- 134. By the time of the arrival of the first units of the Japanese Expeditionary Force on the 23rd August, the Chinese, during the previous ten days, had already displayed clear signs of their inability to undertake offensive operations. Despite the paucity in numbers of the Japanese naval landing party (never more than 6,000 men) who were holding a line from the tip of the International Settlement at Yangtzepoo to the North Station (ex) at Chapei, the Chinese failed completely to dislodge them. To neutral observers this looked ominous. To prevent the Japanese from making full use of the Yangtze and Whangpu Rivers, the Chinese placed booms across the rivers at Kiangyin and at Nantao respectively. These booms served their purpose, but in as far as Shanghai was concerned, a strong boom across the Whangpu River in the vicinity of Wusung would have been far more effective. However, it is quite possible that, by allowing the Japanese navy unrestricted use of the Whangpu as far as Nantao, the Chinese hoped to create trouble with third parties.
- 135. Between the 23rd and 31st August, and after severe fighting, the Japanese Expeditionary Force was successful in gaining a footing on the coast to the north-west of Shanghai between Wusung and Liuho. The Japanese by no means had it all their own way and were made to pay heavily for their success. The Chinese put up a most stubborn resistance, and no quarter was shown by either side. However, by the middle of September the Japanese military forces had succeeded in linking up with their naval compatriots holding the Yangtzepoo-Hongkew area and establishing a continuous line from Wusung to Liuho. For the next few weeks bad weather, the necessity of reorganisation and awaiting the arrival of further reinforcements held up the tempo of the advance. During this time the Chinese forces were given no rest. On both banks of the Whangpu River their lines were subjected to a most unmerciful battering from bombs from the air and shells from the land and river. Speaking generally, the wretched Chinese could only answer with heavy and light automatics and riffe fire. Their artillery was out of date and negligible in numbers, whilst their air force was never in a position to cause the Japanese undue anxiety.
- 136. On the 23rd October the Japanese commenced a general advance. After severe fighting the Chinese were forced to withdraw from Taziang, a strategic point on the Liuho-Shanghai highway. This in turn led to the evacuation of the Chinese positions at Kiangwan, and by the 26th October the Chinese were in full retreat from the Chapei area. With their right flank holding the Soochow Creek, where it adjoins the western boundary of the International Settlement, the Chinese were successful in holding up the Japanese advance until the 5th November. Following up their success, the Japanese crossed to the south bank of the creek, and this spelt the end of organised resistance in the Shanghai area on the part of the Chinese. By the 10th November their link with the settlement had been severed and, hastened by a surprise landing on the coast that the Japanese had successfully carried out on the 5th November, in the vicinity of Chingsanyuen, some 35 miles south-west of Shanghai, they began a hurried retreat westwards. A small force of Chinese troops trapped in the Nantao area were successfully dealt with during the following days.
- 137. The Japanese then turned their attention to the Pootung side of the Whangpu River and, faced with but feeble resistance, they had penetrated, by the 9th November, along the right bank of the Whangpu as far as the Nantao boom, and by the 12th November a small passage had been made through the boom,

thereby allowing their ships to proceed upstream. When hostilities first commenced Chang Chih-chung commanded the Chinese forces on the left bank of the Whangpu, whilst Chang Fa-kwei was in command of the forces on the right With the extension of hostilities it became necessary to bring in a more senior commander in order to ensure co-operation [sic] between the various armies. Ku Chu-tung, one of Chiang Kai-shek's most trusted lieutenants, was entrusted with the task. Many other prominent militarists, such as Feng Yu-hsiang, Chen Cheng, Chu Shao-liang and Pai Chung-hsi were also mixed up in the direction of operations. It is difficult to explain the failure of Chang Fa-kwei to prevent a Japanese landing at Chingsanyuen. For some years previously this part of the coast had been considered particularly vulnerable by the Chinese, and, in consequence, steps had been taken to eliminate the possibility of a surprise landing. Bribery has been suggested, but whatever the cause there is no doubt that this threat to their rear and right flank completed the demoralisation that was now becoming apparent throughout the Chinese forces. To expedite the Chinese retreat the Japanese, on the 13th November, made another successful landing midway between Liuho and Fusan on the Yangtze River. It was a curious form of demoralisation that now set in, because it cannot be said that the Chinese forces ran away or allowed themselves to be caught in a disadvantageous position—they simply vanished. There is no doubt that their morale had been badly shaken, and it is equally certain that they were in no condition to put up any further serious organised resistance against Japanese attacks. From this point of view, it may be said that the Chinese tactics were sound. It is probable that the senior military commanders realised that the will to fight had gone, and that the only thing to do was to save what was possible in the hope of reorganising somewhere well away from the area of hostilities. The advance on Hangchow, Nanking and Wuhu by the Japanese was little more than a march. Threatening Hangehow in the south the Japanese forces by the 30th November had established themselves well to the west of Tai Hu Lake, and by the 2nd December Kiangyin, on the Yangtze, had fallen into their hands. This enabled them to deal with the Kiangyin boom, which was successfully breached by the 10th December.

138. Chinkiang forts, on the Yangtze, held out until the 12th December. Wuhu, some 45 miles south-west of Nanking, was occupied on the 10th December, the capital itself on the 12th December, and Hangchow on the 25th December. The Chinese very stupidly, and against the advice of the German advisers, attempted to defend the walled city of Nanking. Complete disaster to this force was only avoided by the late arrival at Pukow (opposite Nanking) of a Japanese brigade that landed on the left bank of the Yangtze about half-way between Nanking and Wuhu. By the end of December the Japanese had firmly established themselves on the left bank of the Yangtze River at Yangchow (opposite Chinkiang), Pukow (opposite Nanking) and Yuchi (opposite Wuhu). The end of the year saw them in a position to commence a converging attack on Pengpu on the Tsin-Pu Railway and ultimately Hsuchoufu, a very important junction on

the Tsin-Pu-Lung-Hai Railways.

139. From the Japanese military point of view the fruits of victory have been considerable. As a result of approximately six months' military operations in North China, they have succeeded in driving all Chinese military forces from the Provinces of Hopei, Chahar and Suiyuan, and occupying the provincial capitals of Paotingfu, Kalgan and Kweihua. In addition to gaining complete control over the important Peiping–Suiyuan Railway, and setting up a semi-independent Inner Mongolian State (under Japanese patronage), with its capital at Kweihua, they have consolidated their position in the Peiping–Tientsin area; penetrated deeply into the provinces of Shantung and Shansi, and occupied the capitals of these provinces—Tsinanfu and Taiyuanfu respectively. Finally, they have proved that the Chinese armed forces operating in this area were incapable of putting up an effective resistance against an army equipped with modern resources and equipment. It might be added that the Central Government had no intention of despatching its best trained and equipped troops to fight north of the Lung-Hai Railway. These were to be reserved for the Shanghai–Nanking area, and the defence of the Lung-Hai Railway.

140. In Central China they have succeeded in overrunning the most important part of Kiangsu and occupying Shanghai (foreign areas excluded) and the capital, Nanking. In addition, the capital of Chekiang, Hangchow, has fallen into their hands.

- 141. In assessing their successes the following points should be taken into consideration:—
 - (a) The Japanese navy, in addition to establishing an effective blockade of the entire Chinese coast, was able to assist materially the land operations, particularly in the Shanghai area.

(b) The army had almost complete air supremacy and an overwhelming superiority in artillery, tanks and other modern equipment.

142. The Chinese side presents a very gloomy picture. In addition to losing control over the five northern provinces and the south-eastern part of Kiangsu, their most modern divisions have been severely reduced and the navy and air force largely destroyed. Morale has been badly shaken, and for the time being China as a military Power of any importance has ceased to exist.

II.—Foreign Relations.

British Empire.

Coronation of their Majesties King George VI and Queen Elizabeth.

- 143. An imposing Chinese delegation, headed by Dr. H. H. Kung, visited London for the Coronation, and subsequently stayed on in England for several weeks examining industrial questions and possibilities, while Dr. Kung himself was engaged in unsuccessful attempts to pave the way for a British loan to China.
- 144. The actual ceremony of the Coronation was fittingly celebrated throughout China wherever there was a British community of any size.

United Kingdom-General.

- 145. British Troops in China.—In order to give continued effect to the long-standing tradition that the senior (foreign) military officer in Shanghai should be British, Brigadier Telfer-Smollett was given the local rank of major-general in September.
- 146. The question of barrack accommodation in Shanghai (annual report for 1937, paragraph 112) was left in abeyance during the year. Two battalions were accommodated in billets and the third at the premises of the Shanghai Race Club.
- 147. Sino-British Cultural Association.—The new club house in Nanking was opened in February; and a collection of books was presented to the association's library by the British Council. The club house itself survived the tide of war and was reported to be intact after the capture of Nanking.
- 148. British Relief Work in China.—Subscriptions for the Relief Fund raised in London began during the first week in October and contributions continued to pour in. The allocations of the funds to the various relief centres, Shanghai, Hankow, Tsingtao, Tientsin and Canton, were made at weekly meetings of the Central Executive Committee in Shanghai, which was formed by representatives of the British Chamber of Commerce, China Association, British Residents' Association, London Mission, National Christian Council and Executive Committee, in addition, though not directly engaging in relief work, was responsible for relief in the Shanghai area, operating through various subcommittees and making a grant of 50,000 dollars to the Shanghai International Red Cross, as well as smaller grants to other local societies.
- 149. Foreign control over expenditure at the relief centres was exercised by branch committees under the chairmanship of British consular officers. Allocations were made to national societies, British women's associations, the Salvation Army, International Red Cross, British missions and hospitals.
- 150. The original estimate for each centre was: Shanghai $52\frac{1}{2}$ per cent., Hankow, 15 per cent., Tientsin $7\frac{1}{2}$ per cent., Tsingtao 5 per cent., Canton $2\frac{1}{2}$ per cent. of the total fund, with an appreciable reserve. This estimate has proved approximately correct, except that Tientsin received one-quarter in excess of, and Canton three-quarters less than, its estimate.

- 151. Medical supplies, clothing and comforts began to arrive in the second week of December and a committee, which was formed under the chairmanship of the trade commissioner at Hong Kong, distributed large amounts of drugs, instruments, sterilizers and surgical dressings, &c. Most of these supplies went to Hankow (covering five provinces and twenty-three British Protestant Mission hospitals).
- 152. The evacuation of British women and children from Shanghai to Hong Kong involved expenditure from public funds on passages and maintenance in Hong Kong for those in straitened circumstances or without means at all.
- 153. The arrangements for the accommodation of the evacuees were made by the Hong Kong Government in centres, and, in certain cases, by guaranteeing the cost of board and lodging up to 3 dollars a day for those living in private houses. About 80 per cent. of the evacuees were able to look after themselves and were no charge on public funds; others, who stayed in the Government centres, were able—or will be able—to repay the cost of their maintenance. The net expenditure of the Hong Kong Government in this connexion was 152,832·80 dollars (£9,552), which will be borne by the Imperial Exchequer. Further refunds have, however, since been received at Shanghai, and it is estimated that the eventual charge to public funds will be about £6,500. There will also be a charge of about £1,500 for the charter of ships and passages for destitute evacuees.
- 154. In addition to the facilities provided by the Hong Kong Government, a Ladies' Welfare Committee was established in the colony, who disbursed the sum of $13{,}139\cdot75$ dollars, raised by subscriptions and entertainments, on additional comforts, pocket money, &c., for the evacuees in straitened circumstances.

Incidents Arising out of Sino-Japanese Hostilities.

- 155. On the 26th August His Majesty's Ambassador, who was proceeding from Nanking to Shanghai by car in company with the financial adviser and the military attaché, was seriously wounded by a machine-gun bullet fired from Japanese aircraft. This was followed by a bombing attack by a second aircraft from about 200 feet.
- 156. Unofficial expressions of regret were conveyed to different British officials by the Japanese authorities at Nanking, the Vice-Minister for Foreign Affairs at Tokyo, the Japanese admiral at Shanghai, the Japanese Ambssador in London and the Japanese Ambassador to China to Sir Hughe Knatchbull-Hugessen in person.
- 157. On the 28th August His Majesty's Chargé d'Affaires at Tokyo was instructed to present a note to the Japanese Government which recorded the emphatic protest of His Majesty's Government in the United Kingdom and demanded full redress. The note continued by drawing attention to the rule of international law prohibiting direct and deliberate attacks on non-combatants; and emphasised the wider significance of the event. It concluded by requesting (1) a formal apology to be conveyed by the Japanese Government to His Majesty's Government; (2) the suitable punishment of those responsible for the attack; and (3) an assurance that the necessary measures would be taken to prevent the recurrence of such incidents.
- 158. No reply to these representations had been received by the 3rd September, when His Majesty's Ambassador, Sir Robert Craigie, arrived in Japan to take up his post; and in the meantime Mr. Dodds had been informed that, if satisfaction was not received from the Japanese Government, His Majesty's Government would probably decide to recall Sir Robert Craigie. After considerable discussion between the Japanese Minister and Vice-Minister for Foreign Affairs, the Minister of Marine and Sir Robert Craigie, an interim reply, which contained no apology, was received on the 6th September; and Sir Robert Craigie was then instructed to inform the Japanese Government that, if the final reply resembled the interim one, it would not be acceptable.
- . 159. The final reply was received on the 21st September. It contained an admission that Japanese airmen might have caused the "incident," and in these circumstances tendered a formal expression of regret. It added that, if the

identity of the culprits could be established, they would be punished; and stated that instructions had been issued to the Japanese forces to avoid the wounding of non-combatants. This reply was accepted by His Majesty's Government and the incident was regarded as closed.

- 160. It was subsequently announced that Parliament would be called upon to vote a special solatium of £5,000 to Sir Hughe Knatchbull-Hugessen.
- 161. On the 12th October Flight Lieutenant Murray, assistant air attaché, and a party returning from Nanking to Shanghai in a convoy of three cars, were machine-gunned by Japanese aircraft, after full warning of the proposed journey had been given to the Japanese authorities. None of the party was injured, but the car, marked with a Union Jack on the roof, which was carrying Flight Lieutenant Murray, was hit by bullets. Interim expressions of regret were received by His Majesty's consul-general at Shanghai from his Japanese colleague, by His Majesty's Ambassador at Tokyo from the Minister for Foreign Affairs; and by the Commander-in-chief from Admiral Hasegawa.
- 162. On the 27th October Sir Robert Craigie received the reply of the Japanese Government to the official protest which he had made. It claimed extenuating circumstances, but expressed great regret for the unfortunate occurrence; and added that appropriate measures would be taken against those involved in the matter. His Majesty's Government agreed to regard the incident as closed, but Sir Robert Craigie was informed that they would be glad to know in due course what "appropriate measures" had been taken.
- 163. On the 24th October some British subjects riding in the perimeter of the British defence section at Shanghai were attacked, fortunately without casualties, by a Japanese aircraft, which, however, also attacked a nearby British military post, killing one British soldier. The British post retaliated by firing at the aircraft. On the 26th October Sir Robert Craigie received from the Minister for Foreign Affairs the written apology of the Japanese Government, and a promise that the persons responsible would be suitably punished and compensation paid. This apology was accepted by His Majesty's Government.
- 164. On the 29th October three British soldiers were killed and two wounded by Japanese shell-fire in the Jessfield Road area of Shanghai. An apology, with promises of punishment of those responsible and of payment of compensation, was received by Sir Robert Craigie on the 1st November and accepted by His Majesty's Government.
- 165. On the 12th December at Wuhu a British tug, which had conveyed from Nanking His Majesty's consul, the British military attaché and the flag captain to the Rear-Admiral, Yangtze, was attacked by Japanese machine-gun fire after transferring those officers to H.M.S. Ladybird. They proceeded to join the tug in order to protect her, and observed a Japanese field-gun battery firing on merchant ships which were concentrated above the installation of the Asiatic Petroleum Company. Firing continued and was subsequently directed at H.M.S. Ladybird also.
- 166. The latter sustained four direct hits. One naval rating was killed, one seriously injured and there were several minor casualties. A direct hit was also made on the British merchant ship Suiwo. H.M.S. Bee had now arrived on the scene and was also fired upon by the Japanese battery on shore. The commander of H.M.S. Bee immediately landed and protested to the senior Japanese military officer, Colonel Hashimoto, who stated that the firing on the warships was a mistake, but that he had orders to fire on every ship on the river. Subsequently, he stated that if any ships moved on the river they would be fired on, and H.M.S. Bee and H.M.S. Ladybird, after berthing, remained covered by Japanese guns at point blank range.
- 167. Three separate bombing attacks were also made by Japanese aircraft on a concentration of British merchant vessels and H.M.S. *Cricket* and H.M.S. *Scarab*, which were all concentrated in a part of the river previously designated by the Japanese Commander-in-chief as a safety zone.

- 168. A written apology was received by Sir Robert Craigie from the Japanese Government on the 14th November; but on the 16th November he delivered a note drawing their attention to previous assurances that such incidents would not recur, and observing that, as whatever steps they had taken to this end had met with no success, His Majesty's Government must ask to be informed as to the nature of the measures taken.
- 169. A reply to this note was received by Sir Robert Craigie on the 28th December, which, however, contained no indication of disciplinary measures taken against the responsible officers (of whom the principal offender was Colonel Hashimoto), and no reliable indication of guarantees for the future; but suggested that measures of punishment should form the subject of further conversations at Tokyo.
- 170. On the 11th December a revenue protection vessel of the Chinese Maritime Customs, when within British territorial waters near Hong Kong, was fired at by a Japanese destroyer just outside territorial waters. The vessel was then run aground on British territory and abandoned; but the Japanese destroyer subsequently entered British territorial waters and towed the customs vessel off, while a naval party landed and stole chickens. A strong protest regarding this incident was addressed to the Japanese Minister for Foreign Affairs by Sir Robert Craigie on the 22nd December.

New Embassy Site.

- 171. Negotiations for the purchase of the site of the new Embassy at Nanking, which had already dragged on through the whole of 1936, continued unaccelerated in 1937. In slow succession the general terms of the lease, and the purchase price, 260,187 Chinese dollars, to include 100 mow of land, road-making fees, and compensation to dispossessed householders, were agreed upon; but although it was made clear that the money must be paid before the end of the British financial year, the Nanking Municipality was apparently unable to expedite the surveying of the land or the conclusion of terms with the various smallholders concerned. Consequently, as the only makeshift arrangement that could be devised, the cheque was paid to the Waichiaopu on the afternoon of the 31st March, in exchange, not for a lease, but for a note promising the early issue of a lease. Even at this stage the transaction was so ill-defined that provision was made for a further sum of 4,000 dollars, more or less (according to bargaining with those concerned), to be paid later as compensation for removal of graves, destruction of crops, &c.
- 172. In spite of constant pressure on the Waichiaopu and the municipality the next three months led to no visible progress; the cheque was not even cashed till early in July (and then possibly only as a result of a hint that His Majesty's Embassy would have to ask for it back, if the lease was not issued in the near future). However, it appeared that in its own subterranean and dilatory fashion the municipality was actually negotiating with some success, and at the end of the month temporary boundary posts were placed on the site in the presence of a member of His Majesty's Office of Works; and on the 5th August a deed of perpetual lease, together with a plan of the site, was issued. No further mention was made of the 4,000 dollars compensation.
- 173. Since that date political events have prevented further progress, and the position of the provisional boundary posts placed by the municipal surveyors has not been officially checked by His Majesty's Office of Works. However, when conditions in Nanking return to normal, there would be little further difficulty in defining the site, and consideration of the building plans is sufficiently advanced to allow work to be begun at any time.

Kowloon City.

174. The first half of 1937 saw a continuation of the four-year-old disagreement between the Hong Kong Government and the Government of China on the subject of the eviction, for slum clearance purposes, of a number of Chinese residents of Kowloon walled city. The Hong Kong Government had offered such generous compensation, both in cash and in new sites, that by April all but four of the owners of the condemned houses had agreed to move, and it was clear that the refusal of these four was due to official encouragement, presumably from Mr. Philip Tyau, the special delegate for Foreign Affairs at Canton, who had

long taken preternaturally keen interest in the question. The reason for this interest, and for the numerous protests lodged by the Waichiaopu with His Majesty's Embassy, was not that the slum dwellers were being ill-used, but that the Chinese Government was anxious to revive its claim, dormant for nearly forty years, to jurisdiction within the walled city of Kowloon. His Majesty's Government had made it clear in 1899 that they could no longer recognise this claim, and the Chinese Government had tacitly acquiesced in the loss of jurisdiction, but since no renunciation was ever made the Chinese case, based on the convention of 1898, is strong enough to have a good chance of success if it were taken to The Hague Court. For this reason His Majesty's Embassy were in favour of endeavouring to meet Chinese aspirations, whereas the Government of Hong Kong were of opinion that any admission of Chinese jurisdiction inside Kowloon would menace the security of the colony.

175. No final decision on this point has yet been taken, as the events of the second half of the year have relegated the juridical question to the background for the time being; the eviction of the four remaining hovel-owners has also been postponed.

Concessions for Imperial Airways.

- 176. His Majesty's Embassy made frequent approaches to the Waichiaopu with a view to securing concessions for Imperial Airways. One of the objects sought was permission to fly from Hong Kong to Shanghai. The Chinese were at first unwilling to consider this, as they feared it would weaken their position in resisting Japanese encroachments in North China. However, it was pointed out that the two cases were quite different, as Imperial Airways merely wished to fly from a British to a Chinese port, and had no desire to carry passengers or mail from one Chinese port to another. General Ching Kai-shek evidently appreciated the force of this argument, as he subsequently gave verbal assurances that the matter could be arranged. The Chinese Government has, however, now indicated that it would rather not proceed further till the termination of hostilities.
- 177. The second main concession which was sought was permission for Imperial Airways to shorten their route from Penang to Hong Kong by flying over (though not landing in) Chinese territory and territorial waters. The route originally proposed was from Penang to Saigon and thence via Tourane. Later in the year, however, when permission was granted by Siam to fly via Bangkok, Imperial Airways preferred the route through Bangkok, either Vinh or Hanoi, and Fort Bayard, to Hong Kong, and permission was sought for these routes instead of for the Tourane route. The Chinese Government, whose attitude had for years been obstructive, proved to have changed its temper and permission for a period of five years was granted by an exchange of notes on the 18th December. (The permission covers both routes, via either Vinh or Hanoi; there is, in any case, not much difference in the Chinese territory affected.) The first flight of the new service was due to take place on the 19th December, and the present programme is for one flight a week in each direction.

Commonwealth of Australia.

- 178. The Chinese Government sent a national flag and a message of goodwill to the Premier of New South Wales in connexion with the (1938) celebrations of the 150th anniversary of the foundation of Australia.
- 179. The Australian delegation to the conference at Brussels on the Far Eastern crisis was instructed by His Majesty's Government in the Commonwealth of Australia to oppose anything in the nature of sanctions against Japan.

Burma.

180. The Burma-Yunnan Frontier Commission, which, at the end of its first season, had left unfinished the task of deciding on the spot the exact position of the southern portion of the Treaty Line of 1897, reassembled at Laochang on the 1st January, and by the end of April was able to dissolve with its work completed. As was to be expected, the position of the line was not everywhere unanimously agreed upon, and both sides made various reservations to the majority report. However, in order to obtain a settlement the Government of

Burma were prepared to accept the line as it stood, with one exception: they would not in any circumstances give up the Hopang salient, which, though it lay on the Chinese side of the new line, had long been treated as Burmese territory, and which was, moreover, of strategic importance. They suggested the offer to China of Panghung as a fair equivalent, but were prepared, if necessary, to make further concessions.

- 181. The conference in Nanking, which should have been held in the autumn to discuss the findings of the commission, was obviously precluded by the political situation, and His Majesty's Chargé d'Affaires was instructed to suggest to the Waichiaopu that the question should be submitted to arbitration; at the same time he endeavoured to test their reactions to the British claim to Hopang. The Vice-Minister for Foreign Affairs replied proposing conversations between His Majesty's Embassy and the Waichiaopu as a possible substitute for the conference, but adding that he preferred not to be pressed for an early decision. He also conveyed the impression that the Chinese claim to the Hopang salient would be maintained.
- 182. No further progress has been possible, and the matter must now be left in abeyance till the termination of hostilities.
- 183. In the second half of the year the difficulty of importing munitions and other essential supplies by the ordinary routes caused the Chinese Government to take an interest in the possibility of developing communications between Yunnan and Burma. Proposals to build a railway were not received enthusiastically by His Majesty's Government in the United Kingdom, who considered the cost likely to be far greater than could be justified by the economic value of the line. On the other hand, the Government of Burma were willing to co-operate in the establishment of road communications, and have undertaken to build a road to the frontier as soon as the Chinese have built one on their side. Considerable activity took place in the last months of the year, and though no supplies have as yet entered China by this route, it is probable that the road will be open, in the dry season at least, before very long.

Hong Kong (Arms, &c.).

- 184. Though it is only since the outbreak of hostilities between China and Japan that the passage of arms through Hong Kong has become of vital importance, the traffic is far from being a recent innovation. His Majesty's Embassy has for years received frequent notes on the subject from the Waichiaopu, principally on account of the Central Government's anxiety to prevent arms from reaching potentially hostile provincial factions, and its consequent insistence on the production of a Central Government huchao before release of each consignment.
- 185. The recent closure of most other practicable routes has naturally caused a great increase in this traffic, and throughout the autumn His Majesty's Embassy transmitted many requests from the Waichiaopu to the Hong Kong Government, either for the release of arms in advance of the production of huchaos or for the cancellation of huchaos for arms consigned to ports, e.g., Tientsin, that had come under Japanese occupation. These requests were all sympathetically received by the Hong Kong Government.
- 186. Though the passage of arms through Hong Kong is in no way inconsistent with the neutral status of the colony, there was an obvious danger that, if it increased, Japan might put a total stop to it by declaring war on China and exercising a belligerent's right of blockade at sea. His Majesty's Government in the United Kingdom were naturally concerned at this possibility, and also at the deterioration of Anglo-Japanese relations, which was due partly to the erroneous Japanese belief that Great Britain was the principal supplier of munitions to China; and though no legal restrictions were placed on the arms traffic, which continued even after that through Indo-China had (nominally at least) been prohibited, permission was refused for the assembly in Hong Kong of aircraft destined for China. The Colonial Government also declined, in view of the danger of air attack, to allow British rolling-stock on the Canton-Kowloon Railway to leave the British section of the line.

- 187. In addition, it was considered whether Anglo-Japanese relations might not be improved by a public statement showing that Great Britain has supplied only a small proportion of the arms delivered to China via Hong Kong, but it was decided that, while such a statement might do good in Japan, on wider grounds it would be undesirable as emphasising how little Great Britain had done to help the victim of aggression; it might, however, be possible to give the Gaimusho an unofficial intimation of the true position.
- 188. The situation at the end of the year is that, in spite of almost daily air raids, the Canton–Kowloon Railway is still intact and munitions continue to enter China freely; but there are threats of a Japanese landing in South China and it appears probable that they will shortly be able to cut off all communications between Hong Kong and the interior.

Other Countries.

France.

- 189. In pursuance of the Chinese desire for closer relations with Indo-China, the Province of Kwangsi devoted considerable attention during 1937 to the development of communications with that country; and reconsideration was given to the 1914 proposals for a railway line linking Porte de Chine and Nanning and connecting with the Indo-China railway system at Dongdang.
- 190. The French authorities took a very firm line in all matters connected with the protection of their concessions at Tientsin, Shanghai and Hankow. At Shanghai the defence forces in the concession were increased by an Annamite battalion soon after the outbreak of hostilities. In the last stage of the fighting round Shanghai about 4,000 Chinese troops took refuge in the concession, where they were—and remain—interned. Subsequently, the Japanese attempted to assert their right, as conquerors of the Shanghai area, to free passage of troops through the concession, surrender of anti-Japanese agitators, occupation of Chinese official-owned properties, &c. All such attempts were resolutely resisted.
- 191. In response, it is believed, to threats from the Japanese to destroy the Hanoi-Yunnan Railway line, the French Government placed severe restrictions on the use of the line for the transport of munitions.

Germany.

- 192. No completely reliable information was obtainable by His Majesty's Embassy regarding the Hapro-Nanking Barter Agreement (annual report for 1937, paragraphs Nos. 165–167). The military attaché was informed by his French colleague in April that orders for arms and munitions to the value of 45 million dollars had already been placed; and that the remaining 55 million dollars were to be devoted to the construction and installation of the Yangtze steel works.
- 193. A delegation of Chinese industrial experts, headed by Dr. H. H. Kung, visited Germany in the summer in the course of a tour of Europe for the purpose of studying economic developments.
- 194. In October there were in China fifty-nine German military advisers, headed by General von Falkenhausen. The latter, on the outbreak of hostilities, was given virtual charge of operations on the Shanghai front, and it is believed that it was on his advice that General Pai Chung-hsi was sent to the northern front.
- 195. Subsequently, however, his opinions as to the conduct of the war were overruled; and when the generalissimo decided, against his advice, to withdraw his armies from the Shanghai area, the general is believed to have suggested that it might be well to come to terms with the Japanese without delay. Moreover, Chiang Kai-shek insisted on defending Nanking to the last against the express advice of his chief military adviser; and the general, it is believed, was considering very seriously at the end of the year the possibility of withdrawing all the German advisers from China.
- 196. The support, accorded to China by Germany in the form of these advisers and of the importation of munitions, was, of course, in flagrant contradiction of the Anti-Comintern Pact; and proved to be a source of considerable embarrassment to the German Embassy.

197. The mediation of the German Ambassador in connexion with the Japanese peace terms is described in paragraphs of this report.

Italy.

- 198. On the 20th February, during the showing in a Shanghai cinema of a Soviet film on Abyssinia, a party of Italian sailors from the warship *Lepanto* raided the building, burned the film and did damage to the amount of 90,000 dollars.
- 199. An Italian journalist was killed on the 12th December on board the U.S.S. *Panay* during the attack on that vessel; but no protest was made by the Italian Government.
- 200. On the 29th November the Italian Government announced the according of formal recognition to Manchukuo.
- 201. It appears that Italy associated herself with Germany in the latter's unsuccessful attempts at the end of the year to mediate between Japan and China.

League of Nations.

- 202. In accordance with a wish expressed by His Majesty's Government in the United Kingdom, the Chinese Government on the 8th March extended a formal invitation to Egypt to apply for membership of the League of Nations.
- 203. On the 27th September the Far Eastern Advisory Committee of the League passed a resolution condemning the aerial bombardment by the Japanese of such open Chinese cities as Nanking, Hankow and Canton; and agreeing to forward medical supplies for the use of the Chinese people.
- 204. China's appeal to the League against the Japanese aggression, and the events leading up to the convening of the conference at Brussels, are described elsewhere in this report (paragraph No. 58). The conference, after various delays, opened on the 3rd November. Japan and Germany refused to attend, the former on the ground that, as her action in China had been taken in self-defence, it did come within the scope of the Nine-Power Treaty. It was adjourned on the 29th November, in order to afford the Governments concerned time to exchange views, and to explore further ways of settling the dispute. A declaration, however, was approved affirming the belief of the participating Powers in such international instruments as the Nine-Power Treaty; and urging that hostilities should be promptly suspended in the best interests of all nations.
- 205. The League did not meet again between the conclusion of the conference and the end of the year.

United States of America.

- 206. A number of minor incidents occurred in the course of hostilities arising out of the bombing of American vessels and property by Chinese aeroplanes. The most important was an attack on the 31st August by a Chinese air squadron on the steamship President Hoover, which was anchored off Woosung. Direct hits were scored and several persons injured. The Chinese Government immediately expressed regret, and stated that the liner had been mistaken for a Japanese transport. The Chinese Ambassador at Washington also conveyed his Government's regrets to the State Department, and announced their willingness to make full reparation.
- 207. One thousand two hundred United States marines were brought to Shanghai from San Diego in August.
- 208. President Roosevelt's speech in October denouncing the aggressor nations, and Mr. Cordell Hull's subsequent speech accusing Japan of violating the Kellogg and Nine-Power Pacts, proved a source of (temporary) comfort to China.
- 209. On the 12th December Japanese aeroplanes bombed and sank the U.S.S. Panay 28 miles above Nanking. The Panay at the time was convoying three oilers on the Yangtze, two of which were also destroyed. The Panay's boats conveying the survivors and wounded ashore were machine-gunned by Japanese planes. Three foreigners were killed and at least fifteen wounded, several seriously.

- 210. The Japanese version of the outrage which was issued to the press by General Harada was completely devoid of truth.
- 211. Public opinion in America was profoundly stirred, and the exhibition of a film of the outrage which had been taken at the time gave these events great publicity throughout the United States. Though the United States Government eventually accepted the Japanese apologies and considered the incident as closed, anti-Japanese feeling continued at a high pitch, where it was maintained by the evidence continuously produced from American missionary and other sources of the atrocities committed by the Japanese troops.

Union of Soviet Socialist Republics.

- 212. A Pact of Mutual Non-Aggression between China and the Union of Soviet Socialist Republics was signed at Nanking on the 21st August. Its three clauses provided: (a) that neither party should commit an act of aggression on the other; (b) that no assistance should be given to a third party which might attack one of the signatories; and (c) that all existing agreements, bilateral or multilateral, to which the signatories were parties, should remain in force. Mr. Gage was informed by the generalissimo on the 29th August that negotiations for this pact had been proceeding for some time; and had included proposals for a commercial treaty also. The latter, however, had been discarded as no agreement could be reached. Chiang Kai-shek added that the conclusion of the pact did not signify any abandonment by China of her policy of anti-communism.
- 213. Contrary to reports current at the time the pact was signed it does not appear to have contained any clause regarding military or air assistance in the existing hostilities. Indeed, the fact that Soviet Russia gave so little help of this nature was a source of increasing disappointment and resentment to the Chinese Government throughout the year. Various reasons have been suggested for this lack of support, of which the most probable is the known desire of the Soviet Government, having regard to their existing internal troubles, to avoid at all costs any dangerous commitments which might bring them into armed conflict with other Powers, and notably with Japan. Moreover, the possibility should not be overlooked that it is to Russia's interest that China as much as Japan should be weakened, for in such circumstances communism is more likely to flourish; and though as far as China is concerned the activities of the Komintern seem to have been curtailed, it is highly likely that, even if this is so, the curtailment is more than temporary.
- 214. The Soviet Ambassador, M. Bogomolov, left Nanking suddenly at the beginning of November, followed a few days later by the military attaché. It was put about that they had been recalled by Moscow for consultation; but from the time of their departure nothing further was heard of either of them, and the inference is that they were "liquidated." A new Ambassador, M. Luganetz-Orielski, who had been consul at Urumchi, was appointed Ambassador, but had not presented his credentials by the end of the year.
- 215. Shortly after the capture of Nanking the Soviet Embassy was destroyed by fire; and the Japanese were unable to find any explanation of this mysterious occurrence. Another curious case of spontaneous combustion occurred when the new Soviet Ambassador arrived at Hankow to find that his Embassy there had been destroyed in similarly inexplicable circumstances.

International Settlement.

216. The power of the Shanghai Municipal Council to maintain good order and government was tested to the full by the multiple problems arising out of the crisis. The defence of the settlement, the care of vast numbers of refugees and unemployed; the maintenance of the administrative services and police control; as well as the resistance which it was necessary to make to the everincreasing Japanese demands not necessarily formulated in writing, whether for control of the settlement or for full liberty of action for their military forces; all these combined to make the task of the Shanghai Municipal Council a particularly arduous one.

- 217. These difficulties were increased by the closing of that part of the settlement which lies north of the Soochow Creek, which provided diplomatic and administrative problems for the solution of which precedents provided no assistance. Efforts were accordingly made to preserve peace, order and strict neutrality in that part of the settlement which remained under the effective administrative control of the council.
- 218. Emergency Measures.—On the 12th August the council issued orders for the mobilisation of the Volunteer Corps, which at once took up positions in its defence sector. No state of emergency was declared, but a previously prepared scheme of emergency committees was brought into effect.
- 219. On the following day the council requested Brigadier (now Major-General) Telfer-Smollett, D.S.O., M.C., Commander British Forces in Shanghai, as the senior neutral officer, to assume the unified direction of the defence forces of the settlement. On the 15th August curfew regulations were introduced between the hours of 10 p.m. and 5 a.m., subsequently altered to 11·30 p.m. and 5 a.m.
- 220. In order to assist in preserving calm and confidence the council issued official broadcasts nightly from the 19th–31st August in English and Chinese.
- 221. On the 30th August the Shanghai Volunteer Corps was partially demobilised, reverting to the precautionary stage; though complete demobilisation did not take place till the middle of November, by which time fighting had come to an end in the Shanghai area.
- 222. A battalion of Chinese troops, known as the Lone Battalion, after a long resistance in a godown on North Soochow Road, was permitted to enter the settlement and was disarmed by British troops. The council undertook the task of interning those who had entered the settlement until the close of hostilities.
- 223. On the 3rd December, at 11 A.M., despite representations as to the risk involved, and the strain that would be placed on the municipal police, a mixed column of Japanese military units carried out a "Victory March" through the settlement. A hand-grenade was thrown at the procession by a Chinese who was immediately shot by a Chinese municipal policeman. Three Japanese soldiers and three members of the municipal police sustained injuries.

Treaties.

Tabular Statement.

With—.	Place and Date of Signature.	Subject.	Place and Date of Exchange of Ratifications.	Date of Entry into Force.	Remarks.
U.S.S.R	Nanking, August 21, 1937	Treaty of Non-Aggression		August 21, 1937	
Latvia	London, June 25, 1936	Treaty of Amity (see table in Annual Report for 1936, paragraph 181)	London, December 30, 1936	December 30, 1936	
His Majesty's Government in the United Kingdom	Hankow, December 18, 1937	Exchange of notes regarding route to be followed by Imperial Airways services between Vinh or Hanoi and Hong Kong		December 18, 1937	

III.—RAILWAYS.

225. The annual report for 1936 referred (paragraph) to activity in the construction of new railways and in the settlement of indebtedness under old railway loans. This activity continued in the first half of 1937, but the outbreak of hostilities prevented the conclusion of the important contracts for new construction (of lines from Canton to Meihsien and from Pukow to Sinyang, respectively) then under discussion in London. The year ended with most of the railway services in Northern and Central China disrupted.

226. Complete control (in all but name) of the Peking-Mukden Railway was assumed by the Japanese military authorities in July, and though the British employees of the railway remained at their posts their authority was in practice seriously undermined by a large number of new Japanese employees. The Japanese Government refused to recognise any obligation to pay for the use of the line by the Japanese armed forces, and the administration borrowed funds from the South Manchurian Railway to meet running costs and to pay for new works insisted upon by the Japanese forces as military necessities. It is therefore scarcely surprising that in August the administration defaulted on its obligations under the Shanghai-Fengching Mortgage Redemption Loan (£5,000 per month) and under the terms of the settlement of the debt owing to the Metropolitan Cammell Carriage Company (£3,600 per month). In the autumn construction was begun of a line from Jehol to Kupeikou, to be later extended to Tungchow near Peking, and so connected with the Peking-Mukden Railway. As the construction of lines linked to the Peking-Mukden Railway is (under the terms of the 1898 Loan Agreement) the prerogative of the Peking-Mukden Railway Administration, which must apply first to the British and Chinese Corporation for the necessary funds if the administration cannot itself finance such new lines, the corporation requested that representations should be made to the Japanese Government on their behalf.

227. The most important debt settlements negotiated during the year were those for the German shares of the various Tientsin-Pukow Railway loans and advances; with the British and Chinese Corporation for a resumption of payments on the Nanking-Hunan loan of 1916, which had been in arrears since 1925; and for the Hukuang Railway Loan. In view of the serious effects of the hostilities upon railway earnings, it is remarkable that all loan services payable by the Ministry of Railways and due in 1937 were met in full, though it was not possible to write off the arrears which had in some cases accumulated. The defaults by the Peking-Mukden Railway Administration are in a different category, as this line has for some years been semi-independent of the Ministry.

228. In North China the outbreak of hostilities immediately affected services upon the Peking–Mukden, Peking–Suiyuan, Peking–Hankow and Tientsin–Pukow Railways. Although communications on the two former lines were restored fairly quickly, they are still not normal, and on the two latter the advance of the Japanese armies was impeded by extensive destruction of the permanent way and removal of rolling-stock by the Chinese forces. In Central China the Nanking–Shanghai and Shanghai–Hangchow–Ningpo Railways, though bombed almost daily, maintained an extraordinary record of through services up to a few days before the evacuation of the Shanghai area by Chinese troops in November. The completion in the late autumn of the bridge across the Chien Tang River, and of the Chekiang–Kiangsi Railway, made through railway communication possible between Shanghai and Canton via Hangchow, Nanchang, Pingsiang and Chuchow. This greatly facilitated troop movements, and, later, enabled the Chinese to withdraw almost all the rolling-stock (from the Shanghai–Nanking and Shanghai–Hangchow lines) to Central and South China.

229. In the early summer the much-debated loop-line between the Canton-Kowloon and the Canton-Hankow Railways was completed, thus making possible through traffic between Hong Kong and Hankow.

230. Survey and preliminary construction work on the Chungking-Chengtu and Hunan-Kweichow lines was energetically pushed in the first half of the year, but transportation difficulties impeded the work after the outbreak of the hostilities, and at the end of the year there were indications that the Chinese

Government preferred to defer construction of these lines in favour of lines more directly serving strategic needs, such as additional lines from Indo-China, and a line from Hunan to Kwangsi.

231. One of the most striking features of the war in China in 1937 was the failure of the Japanese air force to put the railways out of action. The various administrations, under the supervision of the Ministry, rapidly organised emergency repair departments, and it was seldom that a line was out of action for more than a few hours even after severe bombing attacks. The Ministry of Railways deserves the greatest credit for its success in maintaining railway services and for meeting its foreign loan obligations, in the face of difficulties which were unprecedented in the history of Chinese railways.

IV.—Shipping.

232. His Majesty's commercial counsellor, in a survey made at the beginning of June of the position of British and other shipping engaged in the coastal, river and ocean trades in China, summed up the position as follows:—

(i) On the ocean routes British shipping is at a disadvantage compared with some of its State-aided competitors. Subsidies enable German and Italian express passenger steamships to capture some of the passenger traffic between China and Europe, and subsidies—and possibly cheaper running costs—enable Japanese lines to capture some of the freights on various routes from China.

(ii) On the coastal and river routes British shipping is maintaining its position fairly well, though a few leading Chinese companies are consolidating their position and Japanese shipping interests are making a strong bid to recover some of the ground lost during the

boycott period a few years ago.

(iii) The majority of Chinese companies are very small, with few resources, and short-lived.

The main factors adversely affecting British shipping interests in Chinese waters were, he considered, first, those which were definitely discriminative, benefiting Chinese shipping at the expense of foreign shipping (through bills of lading facilities, facilities for calling at non-treaty ports and discriminatory taxation); and, second, those which operated to the detriment of all important shipping interests and to the advantage of alternative means of transportation (e.g., interport duty). Of these handicaps the one to which the British shipping companies attached the most immediate importance was that which prevented foreign shipping from calling at Laoyao (Lienyunkang), the terminal part of the Lung-Hai Railway. Representations on this subject which had been made to the Chinese Government through 1936 were continued into 1937, but without success, since the Chinese claimed that the area was a military zone. Representations were brought to an end by the outbreak of the hostilities, which, however, brought a fresh crop of difficulties to shipping.

233. The Chinese placed a barrier of sunken ships across the Yangtze at Kiangyin without warning on the 12th August, bottling up H.M.S. Capetown, two British ocean-going steamers and a considerable number of river craft. The larger vessels escaped at the end of December after this barrier was broken by the Japanese in their advance on Nanking, but some of the river craft were deliberately retained by the owners for service in the Middle River, where they were again imprisoned by a new boom placed across the river above Wuhu. While the Kiangyin boom was still unbroken, the two British shipping companies, Messrs. Jardine Matheson and Co. and Messrs. Butterfield and Swire, by a very creditable display of initiative and organisation, managed to operate a through service between Hankow and Shanghai, circumventing the boom by means of cargo boats on the creeks with which this area is mazed. After the fall of Nanking on the 13th December the Japanese regarded the Yangtze between Kiangyin and the new Chinese boom as a military zone and placed obstacles in the way of navigation by neutral ships for purposes of trade.

234. On the 12th August also the Chinese placed a barrier of sunken ships across the Whangpoo above the French Concession at Shanghai so as to prevent

the flank of their army being turned by a Japanese movement along the river. Some neutral shipping was locked in, including one British ocean-going steamer, which got out only on the 31st December.

235. Booms were also thrown by the Chinese across the entrances to Ningpo, Canton and Foochow. The Ningpo boom was, however, never entirely closed and shipping continued to run regularly between there and Shanghai. The Canton boom would have been entirely closed but for the energetic protests of the foreign consular representatives; in the event, it was closed only for a few days of panic; at Foochow the barrier across the river was sufficiently low to permit launches to pass over it, and arrangements were made for shipping to load and unload outside. The entrance to Tsingtao Commercial Harbour was blocked by the Chinese before they evacuated the port at the end of the year.

235A. At Chefoo an attempt was made by the Chinese forces to destroy the mole, in pursuance of their "scorched-earth" policy, but it was only partly successful and did not seriously interfere with navigation.

236. On the 25th August the Japanese naval authorities announced that navigation on the Lower Yangtze and along the Central China coast from Shanghai to Swatow, inclusive, was closed to Chinese shipping. It was explained, however, that since this was not a war-time blockade, foreign vessels could not be seized or compelled to change their course, even if they were carying arms to China, but they might be boarded by Japanese naval officers for the purpose of verifying their nationality in case of doubt. His Majesty's Government in the United Kingdom, without admitting the right of the Japanese Government in the matter, stated that they would, in practice, allow the verification of the nationality of vessels flying the British flag on certain conditions. No serious incidents arose as a result of this arrangement. On the 5th September the blockade was extended northward and southward to cover the whole Chinese coast line with the exception of Tsingtao and the "leased territories of third Powers" (i.e., Hong Kong, Macao and Kwangchowwan).

237. In connexion with the blockade the Japanese Government issued a statement that they would not recognise the validity of transfers of nationality of Chinese ships subsequent to the 25th August, unless the transfer was effected in accordance with the laws of the countries concerned and fully completed. The purpose of this measure was to prevent Chinese vessels from acquiring foreign nationality simply in order to evade the blockade. His Majesty's Ambassador, on the instructions of His Majesty's Government, informed the Japanese Government that if a valid transfer to the British registry had taken place, the fact that the transfer was subsequent to the 25th August was irrelevant; nor could the legal validity of any transfer under English law be determined by any but the British authorities. No difficulties had arisen in connexion with transfers of Chinese vessels to the British flag by the end of the year; indeed, none had been so transferred on the Shanghai register. A considerable number of Chinese craft were, however, transferred to other flags, principally German, Italian and Portuguese.

238. Some Chinese ships (including four purchased by the China Merchants Steam Navigation Company with the assistance of British Boxer Indemnity funds) took refuge in Hong Kong, and a few river steamers, painted to resemble the vessels of one or other of the two British companies, maintained a precarious existence above the Chinese boom on the Yangtze; but apart from these the Chinese merchant fleet ceased to exist: some had been sunk in the construction of the booms, others transferred to foreign flags, the rest taken by the Japanese. As regards Japanese coastal and river vessels in Chinese waters, a number were used by the Chinese in the construction of the booms, a very few were taken over and used on the river. All available Japanese tonnage was used for war purposes, and with the complete disappearance of the Chinese flag from the coast and Lower Yangtze, the British companies and the odd foreign flag vessels obtained a virtual monopoly of the carrying trade in these areas, but it was a precarious and hazardous business with demurrage and insurance charges on the locked-up ships eating up the profits from the occasional fat cargoes obtained on the coast.

V.—MINING.

239. The inadequacy of coal supplied in Japan and the comparatively poor quality of the coal mined in Manchuria is believed to be leading the Japanese to seek new sources of supply in China proper. They are reported, for instance, to be interested in the coal mines at Shihmenchai, in East Hopei, south of the Great Wall, and to have established a company to exploit these mines, and to build a railway connecting them with Chinwangtao. The coal is good quality anthracite. The mines formerly belonged to Chinese, but work in them was suspended on the establishment of the East Hopei Administration. The Japanese are similarly exploring the possibilities of the Chaitung coalfield, to the west of Peking. In October the Hsing Chung Kung Ssu (or China Development Company), which constitutes the spearhead of Japanese enterprise of this nature in China to-day, is said to have bought out the German interests, originally acquired as early as 1898, in the Chinghsing coal mines in Western Hopei. These mines, which are linked by railway with the Chengtai (Shansi) line, have since the Great War been worked as a Sino-German enterprise, and the Japanese are believed to be trying to acquire the Chinese interests also. The output is estimated at over a million tons of bituminous coal yearly, with reserves of between 100 and 200 million tons. The China Development Company also showed interest during the year in the mines of Canton Province, not only coal, but manganese, wolfram, bismuth, &c.

Kailan Mining Administration.

240. The difficulty in connexion with the loan agreement of 1935 between the administration and the Peiping-Liaoning Railway, mentioned in section 223 of last year's report, was satisfactorily settled. On the 23rd April the railway informed the administration that instructions had been received from the Hopei-Chahar Political Council to the effect that, after consultation with the Ministry of Railways, it had been decided that payments of principal and interest on the loan were to be continued as heretofore. The administration therefore resumed deductions of sums due from the Ministry on this account from the freight payable by the administration to the railway, while the administration remained in charge of the rolling-stock.

241. In addition to the perennial troubles connected with the illegal operation of native pits in the mining area, various issues have been raised during the year between the administration, the East Hopei Government and the Japanese military authorities, which are still unsettled. In June, the general manager told His Majesty's Ambassador that the Chinese would endeavour to oust British interests in the administration if and when Japanese political pressure in North China was removed, and that the Japanese for their part would gladly assume control of the mines were it not for the almost insuperable technical and political difficulties in the way of their doing so. In the meantime, the Chinese, for fear of Japanese action, were only too pleased to emphasise the British interest in the administration, and there was no sign that the Japanese had any immediate intention of taking over either British or Chinese interests in the administration by purchase or otherwise. The administration were doing a mutually satisfactory business with Japan, and their relations with local Japanese officials were excellent. The general manager felt that the longer the then indeterminate political situation continued, the better it would be for the administration. As the year closed, however, with the Japanese military grip on the province steadily tightening, while Mr. Nathan was still hoping to settle his difficulties with the Japanese authorities by direct negotiations, he was forced to admit that he might very shortly have to seek the assistance of His Majesty's Embassy, as the local Japanese military appeared determined to ride roughshod over any opposition in North China.

242. The principal questions at issue may be briefly summarised as follows :—

(1) In 1935 certain mining police regulations had been drawn up, under which the East Hopei Government gave the administration the right to organise and control their own police, including the right to nominate and appoint the chief of police. In July the East Hopei authorities

were seeking to have these regulations cancelled, and to appoint their own chief of police. His Majesty's consul-general at Tientsin made representations against such action both to the East Hopei Government and to the Japanese military authorities, and these representations were supported by His Majesty's Ambassador at Tokyo. The administration offered to convert the force into a body of watchmen, armed only with pistols and batons, but strongly resisted the nomination of a chief of police by the East Hopei authorities, who in this matter appeared to have the full support of the Japanese military authorities. No decision had been reached at the end of the year.

(2) Difficulties also arose in connexion with the exploitation of the deposits of fireclay in the mining area which had not previously been worked. These deposits contain a certain proportion of bauxite which the Japanese need for the manufacture of munitions. The Japanese Government are said to aim at obtaining some 200,000 tons of fire-clay annually from East Hopei, and in September the China Development Company began making arrangements for the control of production outside the administration's area, and were seeking a transfer to themselves of the latter's rights of mining fireclay within their area. The administration were not ready to concede their mining rights, but were willing to work in co-operation with the China Development Company, and their own agents in Japan, in the extraction and sale of the deposits. The Japanese military authorities were anxious to acquire sole control of the mining rights, however, and there was a danger that they would not allow the East Hopei authorities to issue the necessary permits to the administration, but would insist on these being given to the China Development Company, which would mean, in practice, a very serious encroachment on the administration's rights over its own property. At the moment of writing, there appears to be some likelihood of an agreement being reached which will be satisfactory to all parties.

(3) In November the administration was informed that the Consolidated Tax Bureau of Hopei, Chahar, &c., was now under the control of the Japanese authorities, to whom the administration was to pay consolidated (or mining products) tax on its coal instead of, as formerly, to the Internal Revenue Administration of the Ministry of Finance at Nanking. The general manager agreed, in principle, that the administration should pay the tax to the *de facto* authority in the area in which the coal was sold, but the Japanese representative of the Consolidated Tax Bureau claimed payment on a different basis from that previously adopted by the Internal Revenue Administration. Pending an agreement, payment of the tax by the administration from the 1st July onwards was held in suspense. Discussions were still in

progress at the end of the year.

(4) The Japanese military authorities are anxious to acquire vacant land at Chinwangtao for the establishment of a military hospital, barracks, workshops, &c. Their requirements in this direction were looked upon with distrust by the administration's local agent, as tending to convert Chinwangtao into a permanent military base. The administration were, however, on weak ground in turning down this request altogether owing to the existence of an agreement of December 1905 by which the Chinese Engineering and Mining Company leased to the Japanese Government certain land occupied by the Japanese forces at that time. A codicil was attached to this agreement to the effect that the Japanese Government having agreed to restore the grounds thus occupied which were not required for military or naval purposes, in the event of military necessity arising in the future that Government might occupy all or part of the grounds so restored, without objection on the part of the company. Some of the land in question had in the meantime been utilised for other purposes, and other sites, which the Japanese considered suitable, were in the middle of the administration's residential area. The administration are, however, seeking to find alternative sites which they can offer to the Japanese for this purpose.

243. In July the administration's agent at Chinwangtao was called upon by Japanese representatives of the East Hopei Customs to allow the berthing at the administration's wharves of vessels employed in the "special trade" of East Hopei, which did not comply with the formalities of, or pay duty to, the Chinese Maritime Customs. The goods carried were believed to be merchandise for sale to the Japanese army, and the vessels concerned had previously landed them at Nanlichuang, where they paid duty to the East Hopei Customs. The administration's agent took the line that he could not allow the use of the administration's wharves by vessels not having a proper discharge permit from the customs, and was supported in this attitude by His Majesty's consul-general at Tientsin vis-à-vis his Japanese colleague. The latter finally issued the desired instructions to prevent the use of the wharves in this way, but queried the right of His Majesty's consul-general to issue instructions to the administration in regard to the disposal of its properties. It was explained to him in reply that the British partner in the administration was subject to His Britannic Majesty's Supreme Court, and that if it appeared to the British consul-general that properties of the administration, held jointly by the British and Chinese partners, were being used for an illegal purpose, the consul-general was entitled to instruct the British partner accordingly and warn him that if he disregarded these instructions, he rendered himself liable to prosecution.

Pekin Syndicate.

- 244. Representations were made to the Waichiaopu, and to the Minister of Finance in person, in March, with a view to putting into effect the arrangements made in July 1936 between the syndicate and the Honan provincial authorities for the repayment of the loan of 300,000 dollars made by the former to the latter in 1925. The Ministry of Finance finally agreed to an adjustment whereby the loan was to be repaid from the National Treasury, in five annual instalments, at the end of each year from 1937 to 1941, all overdue interest being cancelled, and no interest being payable during the period of amortisation.
- 245. With the spread of hostilities between China and Japan the syndicate were nervous that the mines might be bombed by Japanese aeroplanes or occupied by the Japanese forces, or that the Chinese Government might order their destruction to prevent them falling into the hands of the Japanese. Representations were accordingly addressed to the Waichiaopu, while the attention of the Japanese authorities was called to the British interest in the mines and the presence of British employees. Similar representations were made to the Japanese authorities regarding the coal stocks held by the agents of the Chungfu Joint Mining Administration at various points in the area of hostilities, while the same authorities were warned of the presence of armed police at the mines in case the Japanese armies should occupy them.

VI.—TAXATION AND TARIFFS.

Income Tax Law.

246. The principal question of taxation with which the Embassy had to deal in 1937 was that of the application of the Chinese Income Tax Law to British institutions, firms and individuals (see sections 227–8 of last year's report). A note, dated the 22nd January, in the sense of those previously addressed to other heads of missions on the 30th December, 1936, was received by the Embassy from the Waichiaopu, saying that full collection of the tax had begun from the 1st January, and asking that all British subjects residing in China should be directed to conform. The United States Embassy received a similar communication, dated the 27th January. It was decided to make no written reply to this note, but, if necessary, to answer verbally to the effect that the Embassy had repeatedly explained its attitude on the question of taxation, and that it was quite impossible to make the tax binding on British subjects in existing circumstances, but that developments were being carefully watched, and His Majesty's Government in the United Kingdom would adjust its attitude according to the evidence received that the tax was being generally and equitably applied. The United States Embassy similarly made no written reply, but were authorised by the State Department to say that the United States Government's decision in regard to the tax (i.e., that it could not

immediately be applied to United States nationals) had been taken after careful and sympathetic consideration, but that the United States Government would be prepared to give further consideration to the matter in the event of all the Governments concerned acquiescing in the imposition of the tax on their respective nationals.

247. A notice was issued by the Shanghai office of the Income Tax Administration of the Ministry of Finance on the 25th February saying that, in accordance with the Provisional Regulations and Rules governing Income Tax, promulgated on the 21st July, 1936, by the National Government, tax was to be levied from the 1st January, 1937, on three classes of income, derived within the territory of the Republic of China, of all companies, firms and individuals, regardless of nationality. Failure to comply was to be dealt with under articles 18 to 20 of the regulations. At the same time, His Majesty's consuls at various ports received requests from provincial authorities, asking them to instruct British firms and institutions to deduct the tax from the salaries and wages of their employees. Reports from His Majesty's consuls showed that the endeavours of the Chinese authorities to exact payment of the tax from their own nationals were meeting with varying degrees of success, and that there was considerable opposition to it. Moreover, there was some hesitation and delay on the part of certain provinces in complying with the law, presumably because the proceeds from the tax were to accrue to national rather than local revenue. As regards foreign nationals not having extra-territorial privileges, Russians in Shanghai were compelled to pay the tax under threat of the loss of passport facilities, while no attempt was made, on the other hand, to compel German nationals to pay. The principal ways in which it was, as a beginning, sought to make British subjects comply with the provisions of the law were by means of (1) deduction of the tax at source from the salaries of British subjects in the employ of the Chinese Government, railways, missions, universities, &c.; (2) deduction of the tax on the interest on Chinese Government bonds, banking accounts and deposits, and on dividends in Chinese companies; and (3) levy of tax on Chinese in British employment. It was also suggested that British companies in China should deduct tax at source from their shares and debentures, and that British banks should deduct tax on interest on deposits.

248. Many requests for advice as to the attitude to be adopted towards this question having been received by the Embassy, it was felt that, pending full consideration by the Foreign Office, some guidance should be given to His Majesty's consuls. This was done in Embassy circular to consuls, No. 32 of the 31st May. The hope was expressed therein that British communities in China would not content themselves with trying to perpetuate indefinitely their existing privileges, but would seek to meet China's fiscal needs in a constructive manner, seeing that their prosperity ultimately depended on the solvency and prosperity of China. His Majesty's Government were therefore not opposed in principle to the Chinese income tax, but were not prepared to make the tax binding on British subjects by legislation until they were satisfied that it was nondiscriminatory and was being paid by Chinese citizens and other nationals throughout China, a condition which the Chinese were still far from being able to satisfy. Where, however, control of the funds by the Chinese authorities, or the special relationship of the latter with the individual concerned, rendered effective resistance impossible or remonstrance undesirable, as in cases under headings (1) and (2) in the preceding paragraph, it was not the policy of the Embassy to intervene unless there were special circumstances or evidence of discrimination. In other cases, where the tax could not be deducted at source, individuals must estimate for themselves the risks of a refusal to pay, which would obviously vary according to the vulnerability of the individual. In the case of British subjects in the employment of the Chinese Government, railways, &c., it was suggested that they should be confidentially informed that it should be possible to arrange for the tax to be collected on a portion only of their salaries (this was, in fact, successfully arranged in several instances during the year). As regards collection from Chinese employees of British firms, it was not the policy of His Majesty's Government to stand between the Chinese authorities and their own nationals, though British employers were under no obligation to collect the tax. They might, however, supply the names and details of salaries paid to their Chinese employees, and it was suggested that employers might arrange for their compradores, or other principal Chinese employee, to accept responsibility for payment of the tax on behalf of the Chinese staff. As to deduction of tax at source from the shares and debentures of British companies, the latter would first have to seek legal advice as to whether they could be made liable in His Majesty's courts for deductions from dividends made in accordance with the Chinese Income Tax Law. Similarly, as regards deduction by British banks of income tax on deposits, such action, if not taken with the consent of the depositor, might render the bank legally liable in a British court.

249. An interesting point in connexion with the enforcement of the Chinese Income-tax Law is that the Minister of Finance put forward the suggestion that British Inland Revenue officers should assist the Chinese Government in devising a system of income tax administration. It was considered that such an administration, employing foreign experts, should at the outset be under the wing of the customs administration, a precedent for which exists in the postal service, which was launched under the ægis of the customs, and was subsequently made autonomous. A member of the Chinese Coronation delegation spent some time in London during the summer in studying the British system of income-tax administration with the assistance of the departments of His Majesty's Government concerned.

Conservancy Tax at Canton.

A question arose early in the year in connexion with the collection of special dues for local conservancy work at Canton. At the start, these dues were only collected on water-borne traffic, and the British shipping companies protested against this as a further instance of discrimination in favour of rail-borne cargo and said that it would cause a diversion of traffic between Hong Kong and Canton to the Canton-Kowloon Railway. The Embassy were not prepared to resist in principle the collection of a surtax on water-borne cargo for conservancy purposes, as being a matter in regard to which, under the tariff treaties of 1928, the Chinese Government now had full liberty of action. The Japanese and French authorities, however, protested against this conservancy surtax, the Japanese on the grounds of article 1 of the Sino-Japanese Agreement of the 6th May, 1930, the relevance of which was not very obvious, and the French on the grounds of articles 5 and 6 of the Washington Treaty of the 6th February, 1922, and of Annex II (2) of the Sino-French Commercial Treaty of the 22nd December, 1928, which in spirit precludes provincial taxes on trade as well as providing for the abolition of li-kin. Seeing that the contentions of the shipping companies as regards discrimination in the application of the surtax were supported by the Chamber of Commerce at Hong Kong and Canton, His Majesty's Ambassador made representations to the Ministry for Foreign Affairs in line with those already made by the companies to the Inspector-General of Customs. The latter, however, quickly took effect, and the collection of the dues on rail-borne traffic was begun on the 15th April.

Taxes on Oils.

The Government being, as the result of the hostilities, in desperate need of funds, the provincial tax of 1 dollar per unit on kerosene was increased to 2 dollars for six months, or for the duration of hostilities, whichever was shorter. It was stipulated after negotiation that the refund to the companies in repayment of the advance of 5 million Hong Kong dollars made by them in February 1926 to the local Government should remain at 50 cents a unit. About 2,900,000 dollars of the companies' loan of 1926 was outstanding at the end of the year. Earlier in the year the Embassy had had to make representations against illegal provincial levies on oils in Fukien and Szechuan. The Szechuan Provincial Government, however, notified His Majesty's consul-general at Chungking that all local taxation in Szechuan was abolished from the 15th September. This measure, if maintained, could only be regarded as a further step in the fiscal unification of the country, though such taxation was said to be going to be replaced by increasing the business tax to three times its existing scale. Provincial taxation on oils was also abolished in the Province of Kweichow during the year, a further sign of the desire of the Central Government to eliminate provincial levies. Japanese importers in Fukien were believed to be only paying 75 per cent. of the total provincial levy of 1 dollar per unit on kerosene and benzine.

Consolidated Tax on Cigarettes.

252. Early in 1937 the Chinese Government made a further agreement with the China Development Finance Corporation for a loan secured on cigarette consolidated tax stamps to a value of 60 million dollars. Advances were made at 92 per cent. of the face value of the stamps, to be repaid at the full face value of the stamps in seventeen monthly instalments from April 1937 to August 1938. The corporation passed on the greater portion of this transaction to the Chinese banks at the price of 92\frac{3}{4} per cent. of the face value of the security. Such a deal could only be regarded as a very costly form of finance on the part of the Chinese Government. Repayment to the banks was gravely endangered by the taking over of the consolidated tax offices of the Internal Revenue Administration at Shanghai by a Japanese-controlled bureau at the end of December.

253. In April considerable increases were made in the rates of consolidated tax on cigarettes, particularly on the higher-grade cigarettes. Import duties were also subsequently raised to correspond with these higher rates. It was feared by the British-American tobacco interests that these increased rates would greatly increase the competition from illicitly manufactured hand-rolled cigarettes, though all manufacturers of such cigarettes in the interior had been ordered to move to one of four named treaty ports before June 1937, or to close down. Representations against the higher rates of tax were made both by the British and American Embassies, but without result, in spite of the fact that these representations received support from Mr. T. V. Soong, on behalf of the Chinese firm of cigarette manufacturers, the Nanyang Brothers, which he had recently undertaken to reorganise.

Embargo on Export of Chinese Products.

254. Not long after hostilities began, the Chinese Government placed an embargo on the export of a number of products, to prevent their coming into the hands of the Japanese. In September, the authorities of Kwangtung Province suddenly decided to put an embargo on the export of ramie fibre. merchants, who were exclusively interested in the trade in this commodity with Europe, protested through His Majesty's consul-general at Hankow. European interest in this trade was said to aggregate some 6,000-8,000 tons per annum and had the embargo not been lifted the merchants would have been left with very heavy commitments on their hands. Actual commitments at the time were, in fact, computed at 3,500 tons to a value of £140,000. Representations were made by the Embassy to the Waichiaopu at Nanking, and the Ministry of Finance agreed to instruct the Inspector-General of Customs to allow the export of ramie, provided the exporter could satisfy the customs that it was destined for Europe or the United States of America. The export of this, and other commodities, was subsequently rendered very difficult by the blocking of the Yangtze, leaving the Canton-Hankow Railway as the sole means of transport of cargoes to and from Hankow and the central Yangtze area. Apart from the grave risks of interruption of this line, particularly as regards commodities of a perishable nature, further difficulties for exporters arose owing to discrimination in the allotment of cars.

Revision of Import and Export Tariffs at the Northern Ports.

255. At the close of the year, it was reported that the Provisional Government in Peking were about to introduce a revised tariff at the northern ports. His Majesty's Ambassador at Tokyo was instructed to make official representations to the Japanese Government, pointing out that His Majesty's Government attached the greatest importance to the peservation of a unified customs administration for the whole of China, and that the introduction of a separate tariff in the north infringed the stipulations for a uniform tariff at all land and sea frontiers in Annex IV of the Sino-British Tariff Treaty of 1928. These representations were supported by the United States and French Ambassadors at Tokyo. They proved unavailing, however, and the new tariffs were introduced at Tientsin on the 22nd January, 1938, at Chinwangtao on the 24th January, and later at Chefoo and Tsingtao. The object of the revision was said to be the relief of distress of the population in North China, and many articles such as wheat flour, rice and paddy, agricultural and other machinery, were placed on the free list. Drastic cuts in the duties on other articles, such as certain classes of piece-

goods, fishery products, cement, sugar, &c., were, however, clearly designed to assist imports of Japanese products. Altogether, the duties on some sixty items were lowered, the decreases ranging from 7 to 75 per cent. as compared with the same items in the 1934 import tariff. At the same time, the duties on sixteen commodities in the export tariff list were reduced, these, again, being articles of particular interest to Japan.

VII.—TRADE.

Foreign Trade.

256. In spite of the disorganisation of trade caused by the hostilities during the last five months of the year, the total figures of China's imports from, and exports to, foreign countries during 1937 totalled 1,791 million Chinese dollars (roughly £107 million), as against 1,647 million dollars (£98 million) in 1936, i.e., an increase of 144 million dollars (£9 million), of 8·7 per cent.

257. Imports increased from 941 million dollars (£56 million) in 1936 to 953 million dollars (£57 million) in 1937, while exports showed a much larger increase from 705 million dollars (£42 million) in 1936 to 838 million dollars (£50 million) in 1937, thereby decreasing the adverse balance of trade from 235 million dollars (£14 million) in 1936 to 115 million dollars (£7 million) in 1937. The larger increases in Chinese dollars were slightly offset by a small depreciation in exchange.

Direction of Trade.

258. As showing the direction of trade, the following table gives the percentage shares of the principal countries of China's trade in 1937 as compared with 1936:—

	Imports.		Exports.	
	1936.	1937.	1936.	1937.
Great Britain	 11.72	11.70	9.19	9.59
United States	 19.66	19.80	$26 \cdot 40$	$27 \cdot 61$
Germany	 15.94	15.34	$5 \cdot 54$	8.65
Japan	 $16 \cdot 29$	15.76	14 · 45	$10 \cdot 06$
Hong Kong	 1.76	1.83	$15 \cdot 02$	$19 \cdot 38$

To illustrate the direction of trade before and after hostilities began, the following table gives the percentage shares of the principal countries for the first seven, and for the last five, months of the year:—

Imports.

			Jc	unuary-July.	August-December.
Great Britain				11.34	12.78
Japan				18.68	$6 \cdot 12$
United States				18.96	$22 \cdot 33$
Germany				$15 \cdot 20$	15.67
Hong Kong				1.58	3.36
Netherlands East Indies				7.70	10.86
		E	xports.		
Great Britain				8.83	11.21
Japan	1		00	$12 \cdot 51$	4.78
United States				$31 \cdot 67$	18.86
Germany				$9 \cdot 04$	7.78
Hong Kong			10.000	$13 \cdot 49$	$32 \cdot 12$

259. Had it not been for the hostilities, the trade figures for 1937 might well have approached those of the previous record year of 1931, before the world depression had begun to affect this country. By the end of July, imports had gained 36·7 per cent. and exports 45·5 per cent. in comparison with the similar period of 1936. In fact, in the summer of 1937, China's foreign trade was for the first time showing that it had almost completely recovered from the financial crisis of 1934–35, which was caused largely by the exodus of silver owing to the

high price of metal abroad. That crisis ended in the measures taken to stabilise the currency in November 1935, when China "went off" silver, since which date the foreign exchange value of the Chinese standard dollar has been successfully maintained at about 1s. $2\frac{1}{2}d$., with salutary effects on the trade position. The good results of this reform were aided by a bumper harvest in 1936, a factor—in the life of this agricultural country which it is hard to exaggerate.

260. Shanghai's trade has suffered from the present hostilities more than that of other parts of China, owing to the paralysis of communications in the Lower Yangtze Valley and Central China generally. The Japanese blockade of the China coast has intensified the use of Hong Kong's entrepôt services and many cargoes destined for Shanghai have been unloaded in Hong Kong and disposed of from there. Similarly exports from Central China, which normally come down the Yangtze River, have had to find an outlet down the Hankow–Canton Railway to Hong Kong.

Shipping.

261. Foreign (and particularly British) shipping has fully maintained its services on the China coast since hostilities began, and in some instances these services have been increased owing to the withdrawal of all Chinese shipping. Inter-port shipping has, however, to some extent been handicapped by booms placed across the mouths of harbours for defence purposes (e.g., at Tsingtao, Foochow and Ningpo). The port of Shanghai has been unobstructed since hostilities were removed from the Shanghai area. Shortly after the fighting began, the Chinese Government placed an effective barrier across the Yangtze River below Nanking. The British shipping companies maintained regular services above and below this barrier, and even managed to bring a considerable quantity of cargo round it by organising a lighter and launch service by creek and canal. After the capture of Nanking and Wuhu by the Japanese, this latter service could, however, no longer be maintained, and the Chinese Government constructed a fresh barrier higher up the river between Kiukiang and Wuhu. The barrier below Nanking was successfully forced by the Japanese navy, but in spite of this, British shipping services (apart from the collection of produce from a place below this barrier) up-river from Shanghai to Nanking and Wuhu have not been resumed owing, on the one hand, to Japanese opposition on the ground of interference with their military operations, while, on the other, it has not been held desirable to press the issue since the state of desolation at Nanking and Wuhu makes it unlikely that any sort of normal trading can be done for some time to come.

Railways.

262. With the exception of the Canton–Kowloon and Canton–Hankow Railways, most of China's principal railways were at the end of the year completely in the hands of the Japanese army (such as the Shanghai–Nanking, Shanghai–Hangchow–Ningpo, Peking–Mukden, Peking–Suiyuan, Tsingtao–Tsinanfu, and Shansi Railways), or were still involved in the area of actual hostilities, like the Peking–Hankow and Tientsin–Pukow Railways (with sections of the lines in Japanese, and sections in Chinese, hands). Though difficult, owing to interruption from air-raids and the monopolising of rolling-stock for military purposes, the carriage of ordinary commercial cargoes on the Canton–Hankow and Canton–Kowloon lines was still proceeding. On the other railways above mentioned, transportation for commercial purposes had virtually ceased, though the Japanese military authorities had repaired the tracks as they came under their control with considerable speed, a large amount of new rollingstock was being imported from Japan, it was expected that an endeavour would shortly be made to re-establish normal passenger and freight services on several of these lines.

263. The attention of the Japanese consular and diplomatic authorities at Shanghai was called at the end of the year to the large interests of British bondholders in the Nanking–Shanghai and Shanghai–Hangchow–Ningpo lines, and the suggestion was made that those authorities should discuss the future operation of these lines with the representatives of the bondholders in order to secure the uninterrupted service of the obligations secured on them. Up to the moment of writing the Japanese authorities have, however, turned a deaf ear to these suggestions.

Position at Shanghai at end of year.

At the end of the year the trading position at Shanghai was one of waiting. As far as shipping was concerned, all the regular ocean services had been resumed. For the greater part, however, only cargoes of essential commodities, or cargoes that had previously been deviated to other ports (such as Hong Kong, Singapore, Manila, Dairen, or Japan ports) were coming forward. Few new orders were being placed and very little cargo for export was available, owing to the fact that Shanghai was, to a very large extent, cut off from the hinterland in the Yangtze basin, which it normally serves. In the meantime, the deviated cargoes coming forward, or cargoes being released from local wharves hitherto inaccessible owing to Japanese military occupation, were being slowly taken up. Heavy additional charges had been incurred on most of these cargoes for storage, extra insurance and freight, &c., which under the usual form of contract have to be paid by the dealers to whom the goods had already been sold prior to import. Many Chinese dealers were objecting to payment of these heavy charges, while others had disappeared and foreign importers were faced with a difficult task in getting them to live up to their obligations. In the meantime, the industrial districts of Shanghai outside the foreign-controlled areas had suffered damage amounting in many cases to total destruction. The northern and eastern areas of the International Settlement itself, where most of the principal cotton-mills and other industries, besides the most important wharves, are situated, were still under very strict control of the Japanese military and naval authorities, and the re-entry of Chinese was only allowed under permit and in restricted numbers. The result was that few industries in these areas had resumed normal operations, and there was a great deal of unemployment of local labour, to add to the difficulties of the authorities in coping with the vast mass of refugees from the devastated districts outside.

VIII.—Customs.

North China.

265. The occupation by the Japanese army of large areas of Northern China made it quite clear from the outset that serious difficulties were to be expected in connexion with the Customs Administration. It was obviously the fixed policy of the Japanese that no customs revenue should be allowed to reach the Chinese Central Government; and the only doubt was whether the Japanese would allow the existing machinery for revenue collection to continue to function subject to restrictions as to the disposal of funds, or whether they would themselves take over the administration despite the joint opposition of Great Britain, France and the United States, all of whose interests would be seriously compromised by such a step.

266. The main British interests involved were (a) the maintenance of the integrity of the Customs Administration (largely built up by British enterprise) as an efficient fiscal instrument, and (b) the continued service of the foreign loans secured on the customs revenue. These loans were widely recognised as first-class securities and any default in their service would seriously impair the credit of China, the maintenance of which has always been a cardinal point of the policy of His Majesty's Government towards China. It was clear, therefore, that Japanese interference with the customs in North China would seriously imperil both the main British interests in that administration.

267. By the middle of August, the apprehension of the British Chamber of Commerce at Tientsin had been thoroughly aroused; and they therefore proposed to His Majesty's Ambassador the negotiation of an understanding between the Chinese and Japanese Governments whereby the Commissioner of Customs should be authorised to hold all customs collections, earmarked for external and internal loan services, but to make no remittances until the question had been settled between the two Governments. At the same time the China Association in London drew the attention of the Foreign Office to the dangers inherent in the situation.

268. On the 28th August the Japanese consul-general at Tientsin approached Mr. Myers, the Commissioner of Customs at that port, with the proposal that quotas for foreign loans should be remitted but that any surplus should be retained or deposited in the Yokohama Specie Bank pending a general settlement.

The question of internal loan quotas was not to be considered except so far as foreign nationals or groups were concerned. These particular proposals, the commissioner was informed, were for the time to apply only to Tientsin and Chinwangtao; but the Japanese were considering their extension to other ports. In any case, if they were not accepted, the customs would be taken over by the Japanese.

- 269. In the view of the inspector-general these terms were not unreasonable and he suggested to the financial adviser to His Majesty's Embassy that he should be authorised to instruct Mr. Myers to make an informal arrangement on these lines. His Majesty's Government at once instructed His Majesty's Ambassador at Tokyo to remind the Japanese Government of the British interest in the Maritime Customs and its revenues, and to ask for an assurance that that interest would be scrupulously respected. Action on this instruction was taken on the 5th September and on the 7th October the required assurance was given.
- 270. Meanwhile the commissioner at Tientsin, who was being hard pressed by the Japanese military authorities, had reported to the inspector-general that unless a *modus vivendi* on broad lines could be arranged locally, there was a grave danger of the total disruption of the customs in the north. The Chinese Government, however, were reluctant to take a final decision.
- 271. On the 10th September His Majesty's Embassy at Nanking were instructed by the Foreign Office to use their influence "in the highest quarter" with a view to the adoption of the Japanese proposal, which appeared to be the only hope for preserving the integrity of the customs service; and at their discretion to suggest to the Chinese Government that, as a precautionary measure, customs revenues for the whole of China should be paid to the Hong Kong and Shanghai Bank as trustees for the bondholders. The French and the United States Governments declined on the grounds that their interest in the customs was not sufficiently important.
- 272. Mr. Hall-Patch accordingly went to Nanking and urged the desirability of adopting the Japanese proposals in a series of interviews with prominent officials; and Mr. Howe made similar personal representations to General Chiang Kai-shek.
- 273. On the 18th September joint representations were made by the United States Ambassador, Mr. Howe and the secretary in charge of the French Embassy, to the Chinese Minister for Foreign Affairs, whose attitude was that the Chinese Government would consider the proposal sympathetically provided the funds were deposited in a neutral bank.
- 274. However, it soon became clear that the Japanese were not prepared to make any compromise on this point; and on the 23rd September Mr. Myers informed the inspector-general that the only way to maintain the customs service in the north was to agree immediately to the Japanese terms.
- 275. Meanwhile, Mr. Hall-Patch at Shanghai was making every effort to induce the Chinese to give Mr. Myers a free hand, but his efforts were hampered by the division of authority in financial matters and by the quite unfounded suspicions of the Chinese Government that Mr. Myers had allowed himself to fall under Japanese influence.
- 276. On the 28th September the Japanese consul-general at Tientsin urged on his French colleague the imperative necessity of taking an early decision, and suggested that Mr. Myers should act on his own initiative without the authority of the inspector-general, in order to forestall extreme action by the Japanese military authorities, who, being in occupation of North China, claimed that they had every right to seize the customs. For, he said, though they had consented to his arranging matters by negotiation, they could not vary their terms.
- 277. On the 5th October Mr. Howe again spoke to the Minister for Foreign Affairs, on instructions from the Foreign Office, in an endeavour to persuade the Chinese Government to give Mr. Myers a free hand. Similar representations were made by the United States and French diplomatic representatives. Mr. Howe also approached the Minister of Finance in person and the generalissimo in

writing. On the 7th October Mr. Myers received a time limit of two days from the Japanese authorities; and on the 8th October Dr. Wang Chung-hui put forward the following counter-suggestion:—

The Central Bank should nominate the Hong Kong and Shanghai Bank or some other neutral bank as the custodian bank for all customs revenues. The custodian bank should then open an account with the Yokohama Specie Bank for the deposit of the Tientsin and Chinwangtao customs revenues. The Commissioner of Customs should be authorised to draw upon this account for foreign loan quotas and current expenses only, the balance to remain in suspense pending a settlement. This proposal was considered satisfactory by His Majesty's Government in the United Kingdom subject to the receipt of written assurances by the Japanese consul-general regarding the revenues deposited in the Yokohama Specie Bank, and to the funds deposited in the custodian bank being in the name of the inspector-general. By pressure exercised at Shanghai, Tientsin and Tokyo, the Japanese military authorities at Tientsin were now prevented from taking the bit between their teeth, though the Japanese consul-general would only allow three more days of grace, i.e., till the 12th October, on the evening of which day the final Chinese terms (six points) were communicated to Mr. Howe by Dr. Wang. These terms were as follows:—

- (1) All customs revenues should be deposited with the Central Bank of China, which, as a provisional measure, might indicate a bank of a third country as custodian bank to receive them.
- (2) Revenues to include those of Tientsin and Chinwangtao customs.

(3) Authorisation to be given for the duration of hostilities only.
(4) The custodian bank should be responsible to the Central Bank for the safe custody of all customs revenues deposited; but should be permitted to deposit with another bank the Tientsin and Chinwangtao revenues.

- (5) Monthly payments to be continued by the custodian bank; but as regards the revenues temporarily deposited with another bank (as in point (4)) cheques might be drawn on the latter for the payment of the quotas of foreign loans assigned to the two ports and for the defraying of current local expenditure.
- (6) The custodian bank should not concern itself with other matters.
- 278. These terms were received in Tokyo on the 15th October and the Japanese were reported to be taking strong exception to them, chiefly because the arrangement for a custodian bank covered the whole of China, which would nullify Japanese control of the Tientsin and Chinwangtao customs. The Japanese military once more became insistent and Mr. Howe immediately saw Dr. Wang, impressing on him that the only hope remaining of saving the customs was to give Mr. Myers unfettered discretion; following this up with similar representations in an interview with General Chiang Kai-shek. The latter curtly replied that in no case whatever could he agree to handing over the customs revenues to the Yokohama Specie Bank. Nevertheless, Mr. Howe gathered that the generalissimo did not intend to repudiate the six-point terms.
- 279. Mr. Myers, on the 26th October, informed the inspector-general that, being unable to come to any other arrangement, he had decided to use the discretionary powers conveyed to him by Sir Frederick Maze on the 19th October in a telegram (from which as it subsequently appeared that an important word had been omitted). Accordingly, in the face of continued pressure and in order to save the Customs Administration in North China, he informed the Japanese consul-general that, having been authorised to select a bank of good standing for the temporary deposit of the Tientsin and Chinwangtao revenues, he had made arrangements for all purely customs revenues to be deposited in the Yokohama Specie Bank; and that for the time being he did not propose to make any loan withdrawals for either foreign or domestic debt. With this statement the Japanese appeared to be satisfied and the first payments were made into the Yokohama Specie Bank on the 25th October. At the same time, the Japanese issued instructions that all Japanese vessels with the exception of transports should comply with customs regulations and pay regular duties on their cargoes. In this connexion it should be noted that on the 22nd October Mr. Myers, acting on his own initiative and without informing either the inspector-general or the British authorities, addressed a letter to the Japanese consul-general in which he

categorically stated that he would make no remittances for the service of loans, pending a settlement to be reached after the termination of hostilities. This statement was subsequently used by the Vice-Minister for Foreign Affairs at Tokyo in conversation with Sir Robert Craigie as an excuse for not intervening further with the Japanese military authorities at Tientsin.

280. The inspector-general, however, insisted that the Chinese Government might consider that Mr. Myers had acted *ultra vires*; and that therefore unless he could obtain periodical remittances for the service of foreign obligations, he should endeavour again to secure the acceptance of the six-point procedure and in any case to keep the question open. There were indications in Tokyo that the Japanese Government were prepared to consider the six-point proposal on its merits. The military authorities in Tientsin, however, denied all knowledge of this, and further representations in Tokyo were necessary before the Government could be brought to assert control over the actions of the military.

281. However, on the 3rd November, Sir Robert Craigie was informed by the Vice-Minister for Foreign Affairs that there was no chance of a return to the six-point proposal; that the military authorities had accepted Mr. Myers's proposal and that the sums due for the service of foreign loans were being earmarked; while the question of remittance would be settled later.

282. In view of criticisms levelled at Mr. Myers it should be recorded that on the 6th November His Majesty's consul-general at Tientsin reported that he considered him to have dealt with a most difficult situation in the only way possible to save the break-up of the Chinese Customs Administration in North China

283. On the 19th November Reuter's in Tientsin issued a statement that a satisfactory customs settlement had been reached. This premature and incorrect announcement was broadcast the same day by the British Broadcasting Corporation.

284. The question of the Tientsin customs now fell into abeyance until the formation of the Peking Provisional Government on the 15th December. Mr. Myers provisionally and under force majeure accepted the de facto authority of this new régime, without severing his connexion with the inspectorate-general at Shanghai; and the five-barred flag of the new Government was hoisted over the Tientsin customs-house. It appears, indeed, that Manchukuo customs officials (headed by a Japanese who was formerly employed by the Chinese customs) were ready to take over the customs-house immediately, and had Mr. Myers hesitated in accepting the demands presented to him (which almost constituted an ultimatum) a most serious situation would have been precipitated. Similar steps at Chinwangtao were contemplated, and there were indications that the intention was to set up a separate Inspectorate-General of Customs in North China.

285. On the 19th December the Superintendent of Customs at Tientsin showed Mr. Myers a draft proclamation regarding a new tariff which the Provisional Government wished to introduce at that port and Chinwangtao on the 1st January. On the 24th December the British and French consuls-general at Tientsin called on their Japanese colleague and made informal representations regarding the undesirability of any irregular changes in the tariff; but were informed that the existing tariff was unfair to low-priced Japanese goods, and that an immediate reduction in tariff was contemplated on articles of prime necessity for the relief of distress, at Tientsin and Chinwangtao only. Here the matter rested at the end of the year.

Shanghai.

286. About mid-November, it seemed clear that the difficulties encountered in connexion with the Tientsin customs were likely to recur, and in an aggravated form, at Shanghai. It was equally clear that the six-point proposal referred to above would not be accepted by the Japanese in respect of the latter port.

287. The Embassy accordingly suggested some form of international supervision at ports where the Chinese Government were still in control; such as that contemplated in the 1912 Agreement (never abrogated) for the setting up of a Banker's Commission. It was pointed out that the Japanese would find it difficult to refuse to co-operate with other Powers in such circumstances, and

though such a commission would be unpalatable to the Chinese it might preserve the integrity of the customs and prevent the Japanese laying their hands on any considerable surplus.

- 288. On the 17th November Mr. Okazaki informed Mr. Hall-Patch that the Japanese military were pressing for the seizure of the customs, and were being restrained with the greatest difficulty by the civil officials. The latter stressed the fact that any suggestion of a neutral custodian bank for any portion of the revenue would be quite unacceptable to the military, and hoped that British influence would be used to persuade the Chinese to agree to the deposit of revenues in the Yokohama Specie Bank.
- 289. On the 20th November the Shanghai fleet of the Chinese Maritime Customs and a large dredger belonging to the Whangpoo Conservancy Board were seized by the Japanese.
- 290. On the same day His Majesty's Ambassador at Tokyo, on instructions from the Foreign Office, made urgent representations to the Japanese Government against allowing the customs question at Shanghai to be decided under military pressure. He was informed that while instructions had been sent to discuss the matter in a conciliatory spirit, the Japanese military authorities were quite determined that no revenue from the Shanghai customs should reach the Central Government.
- 291. On the 22nd November Mr. Lawford, Commissioner of Customs at Shanghai, was informed by the Japanese consul-general that the intervention of third parties in the dispute was resented, and that unless he (Mr. Lawford) could produce an acceptable plan for the general Japanese supervision of local customs activities, the alternative would be immediate seizure by the army. Mr. Okamoto also emphasised that the appointment of an International Bankers' Commission would not be accepted.
- 292. Meanwhile, the united front presented by the representatives, both at Shanghai and Tokyo, of Great Britain, France and the United States of America and their constant representations to the Japanese authorities, was successful in restraining the military from taking precipitate action. The Commissioner of Customs at Shanghai was, however, subjected to constant pressure by the Japanese authorities to consent to the deposit of the customs revenues in the Yokohama Specie Bank. In the view of the British, French and American Embassy representatives, Mr. Lawford was disposed to exaggerate the danger of immediate seizure of the customs by the Japanese military authorities, and their united efforts were accordingly brought into play with the object of persuading him to use delaying tactics.
- 293. On the 29th November Sir Robert Craigie was informed by the Japanese Minister for Foreign Affairs that official instructions would be sent to Shanghai that the question should be discussed directly with Mr. Hall-Patch, and that full consideration should be given to the views of His Majesty's Government before any arrangement was made with the customs. The Minister, however, would not agree to a proposal made by Sir Robert Craigie for a round-table conference between representatives of Japan, the other interested Powers and the customs; though he insisted that he had no intention whatever of alienating foreign interests.
- 294. On the 30th November Mr. Lawford was informed by the Japanese consul-general that, under instructions from the Japanese Government, he had to ask for accounts to be opened in the Yokohama Specie Bank in the name of Mr. Lawford for the receipt of Shanghai customs revenues (excluding conservancy and tonnage dues); and that he, Mr. Lawford, would be empowered to draw on the Yokohama Specie Bank account for office expenditure. This, the Japanese consulgeneral affirmed, should be done before the matter could be discussed by himself with the representatives of the interested foreign Powers. On representations, however, made by His Majesty's consul-general and the financial adviser, Mr. Okamoto consented to seek new instructions from Tokyo and to reopen the discussions with Mr. Phillips and Mr. Hall-Patch in a few days.
- 295. On the 7th December Mr. Okamoto informed Mr. Hall-Patch that the Japanese Government would give full consideration to the interests of foreign Powers, but could not admit any intervention by them in the discussions between

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himself and Mr. Lawford. Mr. Hall-Patch, after pointing out that the two statements were mutually contradictory, explained that the aim of the Japanese Government, which was to prevent any surplus customs revenue reaching the Chinese Government, would be attained by the Hong Kong and Shanghai Bank (in which revenue other than from Tientsin and Chinwangtao was being collected) holding the surplus from ports no longer under Chinese control in a suspense account; or, alternatively, by some modification of the proposal already made for the establishment of an International Commission of Bankers.

296. The interview was unsatisfactory, though the Japanese agreed to reconsider the question. By the end of December, however, no further steps had been taken in the matter and the question was temporarily in abeyance.

IX.—SALT ADMINISTRATION.

297. On the 1st April the new organic law of the Directorate-General of the Salt Administration, which had been promulgated on the 14th July, 1936, came into effect. By this law the status of the foreign staff was altered from one of conjoint authority and responsibility to one of mere assistance, though in response to an enquiry from the representatives of the interested foreign banks, the Ministry of Finance denied that the law introduced any material change in established practice. A similar assurance was given by Dr. H. H. Kung in London in the course of negotiations for railway loans. Nevertheless, a number of the Chinese district officers and of the Chinese banks interpreted the law to mean what it said, namely, that the status of the foreign officials was altered, and in some cases funds were even transferred without the signature of the foreign officers designated to operate jointly on the accounts.

298. Japanese interests have for some years been endeavouring to arrange for the export of salt from the Changlu district (Tientsin area) to Japan, and on the 10th March an agreement was signed for the export to Japan of 230,000 tons of salt in 1937. Hostilities broke out in North China in July, and on the 5th August the Tientsin office of the Salt Administration (situated in the Italian Concession) was closed and a new office, under Japanese control, opened outside the concession. Control of the salt-producing areas in the Tientsin district has remained in Japanese hands since that date.

299. Elsewhere the effect of the hostilities upon the Salt Administration has been to disrupt district offices and the preventive services in the fighting areas, the policy of the Japanese authorities apparently being to prevent revenues from this source reaching the Chinese Government, rather than to secure such revenues for themselves. At the end of the year Japanese forces controlled, or the hostilities had affected, salt-producing areas normally responsible for half of the salt revenues of the entire country.

X.—FINANCE.

300. The banking structure was generally frozen at the opening of 1937, but the excellent crop of the previous year was having its effects and a general slow "unfreezing" of the banks was taking place, which would have materially contributed to the consolidation of the currency reform. With another good crop in 1937, this process promised to be carried still further and the prospects were fair when the outbreak of hostilities brought all progress to a standstill.

301. The year opened with steadily increasing confidence in the success of the new currency policy, though there was some anxiety over the continued failure of the Chinese Government to organise a Central Reserve Bank, an indispensable feature of the financial reforms if stability of exchange was to be ensured. The mission of the Minister of Finance to Europe in the spring to endeavour to arrange for large loans to back the currency and to finance railway and other construction in China, was seriously hampered by the delay in setting up this Central Reserve Bank, the principles of which were entirely novel to China. Finally, however, after a great deal of controversy, the necessary legislation was passed in June, and would have come into effect but for the outbreak of hostilities in July.

302. Dr. Kung was successful in concluding with British interests a preliminary agreement for a loan of £3 million for the construction of a railway from Canton to Meihsien, and also a preliminary agreement for a loan of £4 million for a railway from Pukow to Sinyang. Negotiations for a currency loan of £20 million were also far advanced when the crisis in North China put an end to the discussions. Dr. Kung's activities in Europe and America were watched with close attention by the Japanese Government, which was disposed to accept without protest the loan for the Canton-Meihsien line, but disapproved of the conclusion of an agreement for the Pukow-Sinyang line without the approval of other members of the consortium, and was most suspicious of the negotiations for the currency loan.

303. The budget estimates for the year the 1st July, 1937, to the 30th June, 1938, balanced at a little over 1,000 million dollars, but these related only to the receipts and expenses of the National Government, and, in the absence of reliable information concerning provincial and local budgets and of the mutual financial arrangements between the National Government and the provinces, the national budget was of importance and interest mainly in so far as it represented a further stage in the process of introducing modern accounting and budgetary methods

into Chinese official finances.

The outbreak of hostilities in North China led to a shortage of legal tender notes in that area and diminishing confidence in locally issued notes. There were also heavy purchases of foreign exchange, which unsettled the market to some extent. Increasing tension in the Shanghai area early in August prompted heavy withdrawals from Chinese banks and further demands for foreign currency, and on the actual outbreak of fighting in the Shanghai area the general unsoundness of the Chinese banking structure was made manifest. Amongst the many temporary remedies suggested were a moratorium on foreign payments, exchange control, repudiation of the northern note issues and a dual currency. On the 13th August the Chinese banks were ordered by the Government to close for two days. British banks in Shanghai, who were in a very much stronger position than the Chinese banks, were anxious to remain open as long as possible, but on account of the difficulty in obtaining notes and foreign exchange cover it was obviously impossible for them to remain open for more than a few days if the Chinese banks were closed. Steps were therefore taken by the issue of a King's Regulation to authorise them to consider as bank holidays (if they wished to do so) all days on which the Chinese Government banks remained closed.

305. The Chinese banks, however, opened again on the 16th August, with severe restrictions on withdrawals of existing balances in cash. At the same time, a new currency ("Hui Hua" or "Transfer Dollars") was introduced for the purposes of inter-bank settlement. On account of the difficulties of adjusting the Chinese banking system, a crisis (such as the one which arose at this time) could have been met in only two ways—interference with the currency, or interference with the banks—and the latter policy was adopted. The freezing of deposits in the Chinese banks, the rigid control on inter-bank payments, and a "gentlemen's agreement" amongst foreign banks not to accept new Chinese accounts proved for a time highly successful in maintaining the exchange and general confidence in the currency. The stagnation of the import trade also assisted the exchange position by lessening the legitimate demands for foreign currency.

306. The conflict of opinion between the Shanghai banking interests—mainly representing orthodox financial views—and political interests in Nanking became acute in September, though at the end of the year orthodox views still prevailed. An attempt to float a large internal loan, "Liberty Loan," in August by the Minister of Finance was not a success, and as means were devised to evade "Transfer Dollar" restrictions (by discounting for cash), the influence of the orthodox financiers inevitably waned.

307. At the end of 1937 the position, therefore, was that, despite the hostilities, the external value of the Chinese dollar was still maintained, but only by means of restrictions which were becoming increasingly difficult to enforce. Tax collections were seriously affected, and for purchases of arms and munitions it was freely rumoured that the Chinese Government was drawing upon its exchange reserves. Estimates of these and of the note issues varied widely, but it is probably true to say that the ratio of reserves to note issues at the end of

the year was about one to three, and that reserves in foreign currencies and silver totalled about 600 million dollars, against a note issue of about 1,800 million dollars. Whilst China deserves the greatest credit for maintenance of her credit and the exchange in the face of most serious difficulties, it must be admitted that this was to some extent artificial.

XI.—AVIATION.

308. Largely due to the influence and energy of Mme. Chiang Kai-shek, the Aeronautical Affairs Commission made great efforts during the first six months of 1937 to reorganise the Chinese air force. The sum of 84,390,000 dollars was budgeted for the air force during the financial year 1937–38, some sixty-eight obsolete types of aircraft were written off, and the number of squadrons was reduced from thirty-one to twenty-one in order to bring them to a state of efficiency for war and to enable the maintenance of a reserve supply of aircraft for each squadron. In addition, a comprehensive Five-Year Plan was drawn up with a view to the provision of a first-line strength of 1,000 aircraft at the end of this period. The plan also provided for the establishment of an aircraft and aero-engine industry in China which would enable the Aeronautical Affairs Commission to be independent of foreign sources of supply, and a scheme was also prepared for an Air Zone Organisation which divided the country into six air zones, with the object of decentralising the command and administration of the Chinese air force. Owing to the outbreak of hostilities in July little progress was made in developing this plan.

Aeronautical Affairs Commission.

309. The internal organisation of the Aeronautical Affairs Commission was revised in April, the main changes being that the members of the Standing Committee were reduced from five to three and a Purchasing Committee was formed which was to be responsible for the purchase of all aviation supplies and equipment. Previously the Aeronautical Affairs Commission had no direct control over aircraft purchases, which were effected by the Central Trust, and it was hoped that, by means of the new organisation, better value would be obtained and the illegal commissions which had been prevalent in the past would be prevented.

Foreign Air Advisers and Instructors in China.

310. Wing Commander G. Malley, M.C., A.F.C., remained as foreign adviser to the Aeronautical Affairs Commission. With the Italian support of Japanese aggression in China, the opportunity was taken to eliminate Italian influence, and in November General Scaroni and the remaining members of the Italian mission returned to Italy.

Aircraft Factories.

- 311. The contract with the Curtiss Wright Aircraft Factory at Hangchow was prolonged in September for a further two years. Owing to its liability to attack by carrier-borne aircraft, the factory was transferred partly to Nanchang and partly to Shiukwan prior to the outbreak of hostilities.
- 312. On the completion of the Sino-Italian National Aircraft Works, Nanchang, work was in progress on the construction of "Breda" type aircraft, but, with the elimination of Italian influence, construction of more up-to-date military types of non-Italian manufacture has been started. Production at this factory was greatly hampered by repeated Japanese bombing.
- 313. With the move of part of the Hangehow Aircraft Factory to Shiukwan, the factory there assumed an important position as a means of supplying the Chinese air force with equipment. Due, however, to the length of time required to transport and erect the necessary machinery, few aircraft were completed. The situation was further complicated by the unwelcome attentions of Japanese bombers.

Flying Training Schools.

- 314. During the first six months of the year the three flying training schools were busily engaged in training pilots. Advanced training only was carried out at Hangchow, pupils undergoing their elementary training at either Lovang or Canton.
- 315. The Chinese were seriously concerned as to the vulnerability of Hangchow to air and sea-borne attack and, on the outbreak of hostilities, the flying training school was transferred to Loyang. Unfortunately, Loyang proved to be within the range of the Japanese advance in the north and the school was eventually transferred to Kunming (Yunnanfu), where pilots are now receiving advanced service training. Elementary flying training is being carried out at a flying training school established at Liuchow (Kwangsi).

Kwangsi Air Force.

- The Kwangsi air force, in spite of financial difficulties, managed to retain its identity as a separate air force and comprised some sixty obsolete aircraft mainly of British types, with a few Japanese single-seater fighters and French advanced trainers. These, despite their age, were kept in good condition by efficient ground personnel. There are two service squadrons, one stationed at Nanning and the other at Wong Min.
- 317. It is reported that, when hostilities commenced, there was considerable friction with the Aeronautical Affairs Commission, who wished to take over entire control at Liuchow, then the headquarters of the Kwangsi air force. A compromise, however, was reached by which all aircraft, personnel and equipment were transferred to Nanning, leaving the Aeronautical Affairs Commission in control at Liuchow.

Aircraft (China) (Limited).

318. At the commencement of the year, the four principal British firms in Shanghai representing aviation interests in China) combined as "Aircraft (China) (Limited) " in order to avoid the unnecessary competition which had arisen in the past. Simultaneously, a group comprising most of the British aircraft and engine manufacturers was formed in England with the object of obtaining a share in the Chinese market through the medium of Aircraft (China) (Limited). This company was successful in negotiating a number of orders for British aircraft but, owing to the situation created by the expansion of the Royal Air Force, only a small number of these orders could be met. The company also tendered for the construction of an aero-engine factory in China, which project, owing to the hostilities, is now in abeyance.

Sale of Aircraft.

- 319. Following on the protracted negotiations mentioned in paragraph 290 of last year's report, thirty-six Gloster "Gladiators," three de Havilland Rapide Ambulance aircraft and three de Havilland Rapide Passenger aircraft were sold to the Central Government. Earlier in the year two Airspeed "Envoys" were sold to Kwangsi and were flown out in record time from England.
- 320. Subsequent to the outbreak of hostilities, extensive orders for foreign aircraft and engines were placed with the United States of America, Germany and France, though few of these aircraft had arrived in China by the end of the year, which was due partly to the blockade instituted by the Japanese. Nineteen Martin Bombers, purchased from the United States of America, were held up at Manila, owing to the fact that the United States Government refused permission for them to be erected there and flown direct to China; but arrangements were subsequently made for them to be shipped via Hong Kong to Canton for assembly. It was reported that the French had made arrangements to deliver forty Dewoitine Fighters and forty Amiot Bombers via Indo-China.

Sino-Japanese Hostilities: Air Aspect.

321. At the commencement of hostilities, the Chinese air force had a strength of 369 service type and 305 training type aircraft, of which number only 220 were serviceable and fully equipped for war purposes when operations commenced. It was the announced intention of the Chinese to conserve this striking force until it could be employed to deliver an effective blow. Unfortunately, this plan was not adhered to and the majority of these aircraft were wasted in the first month of the conflict, due partly to lack of flying experience and partly to the complete absence of even an elementary knowledge of the employment of aircraft in war. Although confronted by slow out-of-date Japanese Naval Air Service types, the Chinese failed to make use of their superiority in performance, except in the defence of Nanking and Hangchow areas, and at no time was an energetic offensive attempted. The Chinese success at Nanking and Hangchow was largely due to the fact that the Japanese bombers were slow and were operating from air bases situated a long way from the targets they were attacking.

- 322. The Chinese were singularly unfortunate in their selection of targets. They repeatedly attempted to bomb the Japanese flagship *Idzumo*, and failed to attack the large concentration of transports and other ships anchored off the entrance to the Yangtze. Their initial attacks on the 14th August proved disastrous to the International Settlement of Shanghai, where several badly aimed bombs killed 1,500 people in the crowded streets and wounded over 2,000 others. These incidents were responsible for the decision to evacuate foreign women and children from the settlement, while the unintentional bombing of neutral shipping in the Yangtze caused all ocean-going vessels to suspend sailings to Shanghai after the evacuation.
- 323. After the first four weeks of hostilities, the Japanese had prepared aerodromes at Point Island (Shanghai) and on Tsungming Island, from which they were able to operate all types of aircraft. Large bomber formations, escorted by fighters, were employed against Nanking, but, owing to an excellent system of air-raid warnings and extensive system of dug-outs, casualties were not heavy. As a result of representations by foreign Powers, the Japanese ceased bombing targets in the city of Nanking and confined their attacks mainly to the military aerodrome to the south of the city.
- 324. Opposition from Chinese fighters gradually diminished, although the anti-aircraft defences proved accurate enough to cause the Japanese pilots to operate at high altitude with resultant loss of effective bombing aim. Chinese attacks continued to be delivered at night by single aircraft on Japanese positions along the Whangpoo River front and on the Point Island aerodrome, drawing an intensive but ineffective anti-aircraft fire from the numerous Japanese warships. Bombs were dropped indiscriminately at night, and considerable damage was caused to foreign property along the river front.
- 325. With the loss of most of her original equipment China made strenuous efforts to purchase new aircraft in America, France, Germany and England, but the blockade of the Chinese coastline restricted the ports of entry for such supplies to Burma, Indo-China and Hong Kong. Twenty, out of an order for thirty-six Gloster "Gladiators" ordered by China in August, arrived in Hong Kong in November. These aircraft were despatched by rail to Canton, where they were erected and flown into the interior. Approximately 150 aircraft were flown by Soviet pilots to China from the Union of Soviet Socialist Republics via Lanchow, and further supplies continued to arrive.

Civil Aviation.

326. Both the China National and the Eurasia Aviation Corporations extended their services and considerably increased their traffic up to the outbreak of hostilities, when all civil air services in China were either suspended or seriously curtailed. Consequently, what might have been a record year for air transport in China, ended with disastrous losses.

XII.—LEGISLATION.

327. The question of the Draft Constitution, which had been postponed indefinitely in 1936 (see paragraph 317 of the annual report for that year), was revived at the third plenary session of the Central Executive Committee in

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February 1937, when a resolution was passed that the National People's Congress should be convened on the 12th November, to enact the Constitution and decide the date for its enforcement. Certain amendments to the Draft Constitution, as well as to the legislation governing the organisation and election of delegates of the congress, were thereupon submitted to the Legislative Yuan for consideration, being eventually adopted without a substantial alteration. The details of these amendments were reported in Nanking Embassy despatch to the Foreign Office, No. 54, of the 18th May. Owing to the state of emergency resulting from the subsequent outbreak of hostilities between China and Japan, the Chinese Government was compelled to order the postponement of the congress sine die, and the issue is therefore once again in abeyance.

- 328. The revised versions of the Insurance Law, and the Insurance Business (or Enterprises) Law, referred to in paragraph 319 of the annual report for 1936, as well as of the Insurance Business Law Enforcement Law, were promulgated on the 11th January. The dates upon which these three measures were to come into operation, were to be announced by separate mandate, which, so far as is known, is still pending.
- 329. The Provisional Measures for the Punishment of Bandits and Brigands, which were issued on the 31st August, 1936, as a revised form of an equivalent Act of the previous year, with a limited term of application of one year, were revived for a further similar period by a National Government mandate of the 31st August, 1937.
- 330. The principal measure relating to narcotics to be recorded was a mandate of the 22nd September, transferring the control of the General Association of Opium Suppression Commissions of the Military Affairs Commission to the Executive Yuan.
- 331. The most important judicial measure during the period under review was the promulgation, for immediate enforcement, on the 8th January of the Administrative Procedure Law and the Law Governing Appeals against Administrative Measures. These laws were, in effect, amendments of two laws promulgated in 1932 under the titles of the Administrative Actions Law and the Law of Petitions and Appeals, which were thereby superseded.
- 332. Of the numerous other Acts subjected to amendment during the course of the year, the most noteworthy were the Press Law (or Law of Publications) of 1930, revised on the 8th July, a translation of which was subsequently published in Volume XXI of The National Government's Laws and Regulations series, issued by the British Chamber of Commerce at Shanghai; the Chambers of Commerce Law revised on the 19th January; the Agricultural Associations Law, accompanied by an Enforcement Law on the 21st May, for immediate application; and the Strategic and Fortified Zone Law of September 1931, which was amended on the 27th September, 1937, so as to include an aerial zone among the prescribed prohibited areas.
- 333. As might be expected, while the legislation passed during the first part of the year, apart from constitutional, judicial and general measures, dealt for the most part with administrative reforms and economic reconstruction, the tenour of legislative production during the period following the Lukouchiao incident in July was predominantly military.
- 334. A considerable number of the early measures were devoted to the development of agriculture and husbandry, and included the issue of a mandate on the 25th June putting into effect, as from the 1st September, the Granary Enterprises Law of the 9th May, 1935, together with the Granary Enterprises Law Enforcement Ordinance, promulgated on the 10th March, 1937.
- 335. Economic and financial legislation includes the extension for another year of the Provisional Ordinance for the Punishment of Evasions of Customs Duties (see paragraph 322 of previous report) by mandate of the 3rd July, for the protection of the customs revenue; the promulgation on the 15th July, for enforcement during a period of two years from that date, of the Provisional Ordinance for the Punishment of Offenders Impairing National Currency, with

a wider range of restrictions to safeguard the currency than were contained in the similar act of 1935, now superseded; and the elimination in February from the schedule of stamp-tax rates of the discriminatory exemption previously accorded to bills of lading issued by the Government-operated China Merchants Steam Navigation Company. The rate of the stamp-tax was subsequently doubled respect of a large number of items, and increases made in the scale of fines, &c., under the terms of the Provisional Measures Governing the Collection of Stamp-Tax during the Emergency Period, issued by the Ministry of Finance on the 11th October. This was, however, as the name implies, one of the special war-time measures of the latter half of the year (and without any preferential purpose), and will presumably be rescinded on the termination of the crisis.

The following are representative of the numerous military measures passed during the year (besides the increase of the stamp-tax and revision of the Strategic and Fortified Zone Law already referred to). The National Citizen Labour Conscription Law and the Military Requisition Law, both promulgated in July, though there appears to be no record as to the date of their actual enforcement, are supplementary to the Conscription Law of 1933, the enforcement of which, on the 1st March, 1936, was reported in paragraph 321 of the annual report for that year. Acts of insubordination or otherwise detrimental to the Chinese military forces were made punishable, in many cases by the death penalty, by the War-Time Military Law of the Republic of China and its Enforcement Ordinance, both promulgated on the 24th August for immediate enforcement. The scope of military jurisdiction over subversive or otherwise disloyal elements of the population was further extended by the revised Emergency Law for the Punishment of Offences against the State, promulgated on the 4th September, to supersede forthwith the ordinance issued on the 31st January, 1931, under the same title. Severe penalties for exporting food-stuffs to the Japanese were provided for in the Provisional Ordinance Governing the Punishment for Supplying the Enemy with Grain, promulgated and enforced on the 1st September. The procedure for the importation and movement of war material was expedited by the revision on the 30th August of the National Government Rules for Permits Governing the Transportation of Military Supplies and the respective Detailed Enforcement Rules, originally promulgated on the 31st December, 1929. Special Provisional Measures Governing Exemption from Import Duty of Medicines for the Use of Wounded Soldiers and Civilians were jointly issued at the end of the year by the Ministry of Finance and the National Health Administration to facilitate measures of relief.

337. Mention should be made in this connexion of the reorganisation of the Military Affairs Commission into the equivalent of a War Cabinet with five specialised departments, and the reorganisation, in the process of more efficient centralisation, of the functions and structure of various subordinate Ministries of the Executive Yuan. In the absence, however, of any recent Central Government Gazettes, the receipt of which, in North China, completely ceased in mid-August, the records as to the dates and relevant legislative authority for these organic readjustments are incomplete.

338. In conclusion, reference should be made to the legislation passed with respect to North China by the "bogus" administrations established in the wake of Japanese military occupation. The measures passed first by the various so-called Local Peace Maintenance Associations, and notably by those at Peking and Tientsin, and subsequently, in the early stages of its existence, by the Provisional Government of the Republic of China, which took over the supreme administrative control in mid-December, were merely of local application and there is no need to recapitulate the particulars already contained in Peking despatch to the Foreign Office, No. 1179, of the 30th December. As a general rule, it may be stated, in so far as normal civil and criminal jurisdiction is concerned, these new administrations continue up to the end of the year to apply existing codes of the Central Government, but there were indications that the Provisional Government intended to repeal or modify certain other national legislative enactments, such as those specifically relating to anti-Kuomintang and other subversive activities directed against the Nanking Government, the application or quotation of which in their existing form was likely to be a source of trouble or embarrassment.

XIII.—CLAIMS.

Outstanding Claims.

Sinkiang Claims (paragraph 338, annual report for 1936).

339. On the 19th June Sir Hughe Knatchbull-Hugessen left with the Vice-Minister for Foreign Affairs a memorandum stating that His Majesty's Government would waive compensation for material losses if the Chinese Government would make an ex gratia payment in respect of the British subjects who lost their lives. Mr. Hsu Mo informed Sir Hughe that he saw no prospect of this proposal being favourably entertained. Nothing further has been heard of the matter.

Hankow Electric Light and Power Company's Claim.

340. The original claim against the Hankow municipal authorities for current consumed was for 59,366·70 dollars. This was subsequently reduced to 23,204·44 dollars. Against this, however, was a claim by the Wuhan Telephone Administration for excessive current charges. After some negotiation, it was agreed to offset the two claims, and cancel the sum of 20,164·71 dollars on both sides. In addition, however, the Telephone Administration claimed 7,243·53 dollars interest. This was, in turn, offset against arrears of payment due to the company totalling 8,091·07 dollars, and on the 20th February His Majesty's consul-general, Hankow, reported that the case had been settled by the payment to the company by the administration of the difference of 847·54 dollars. This may be regarded as a very satisfactory settlement.

Claims Arising from Sino-Japanese Hostilities.

- 341. On the 23rd August Sir Hughe Knatchbull-Hugessen informed the Waichiaopu, on instructions, that His Majesty's Government must reserve all rights as regards holding the Chinese Government responsible for damage or loss to British life or property as a result of action taken by Chinese forces during the present hostilities in China.
- 342. More detailed information as to the attitude of His Majesty's Government was subsequently available, and instructions were issued that claims were to be considered as falling into three classes as follows:—

(1) Illegal action by military, such as looting.

(2) Wanton or negligent damage not justified by military necessity.

- (3) War damage due to normal shelling or other military operations, or due to military necessity.
- 343. It was at first decided that only claims under classes (1) and (2) were presentable, and that those under (3) were not, except in cases of occupation of British premises amounting to requisitioning. In November, however, this ruling was modified, and it was decided that class (3) claims should be included in the lists being prepared for ultimate presentation, though there was little prospect of their being paid. It was also decided that claims for denial of access to property (of which there were many in Shanghai) might be accepted if direct, and not consequential.
- 344. In December a Claims Office was set up in the Shanghai consulate-general, and at the beginning of that month had already received some 200 claims.

Minute Paper.

Register No.

P. 2.

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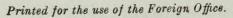
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Sir H. Knatchbull-Hugessen to Mr. Eden.—(Received May 18.)

(No. 368.)

Sir, WITH reference to Mr. Howe's despatch No. 420 of the 21st April, 1936, I have the honour to transmit to you herewith the annual report on China for the year 1936. I am indebted for the preparation of this report to the members of the staff of this Embassy, who have all excited in the considering of the staff of this Embassy, who have all assisted in the compilation.

I have, &c. (In the absence of the Ambassador), B. E. F. GAGE.

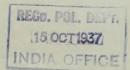
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I.—INTERNAL POLITICAL SITUATION.

(1) General.

THE outstanding features in the internal political situation in China during the year 1936 have been, firstly, the continuation of the Japanese pressure on the Central Government and the northern officials, accompanied by the use of officially protected smuggling as an instrument of policy; secondly, the south-western coup d'État followed by the reunion of Canton and Nanking; thirdly, the strange affair of the arrest of General Chiang Kai-shek and other leading officials by the Young Marshal; and lastly the growth of a national sentiment and the revival of national self-confidence after the sad battering which it had, over a period of five years, received at Japanese hands.

- 2. Sino-Japanese relations are dealt with in a separate section, but it will be difficult to keep them altogether out of the present section inasmuch as there was hardly a political event of any importance which was not affected in some way by the nature of China's relations with Japan.
- 3. The composition of the Kuomintang party and Central Government organs has remained practically unchanged throughout the year. It will be remembered that after the meeting of the Fifth National Congress of Kuomintang Delegates in November 1935 and the attempted assassination of Mr. Wang Ching-wei a general reorganisation took place. Though Mr. Wang Ching-wei's name was retained on the Central Political Council and the Standing Committee of the Central Executive Committee, his place as President of the Executive Yuan was taken by General Chiang Kai-shek, who, combining that post with those of chairman of the Military Affairs Commission, vice-chairman of the Standing Committee of the Central Executive Committee and vice-chairman of the Central Political Council, became more indisputably than ever the dominating figure in Chinese national life. The Japanese-trained and Japanese-speaking element in the Cabinet was at the same time strengthened with a view to creating a more favourable atmosphere for the Sino-Japanese discussions which it was hoped to initiate. Of the twelve major posts in the Government, six, including the Ministries for Foreign Affairs, Interior, War, Industry and Railways, were now in the hands of men who had received their education in Japan.

4. The following is a list of the holders of the principal party and Government posts at the beginning of the year 1936:—

Standing Committee of the Central Executive Committee—

Hu Han-min (chairman).
Chiang Kai-shek (vice-chairman).
Wang Ching-wei.
Feng Yu-hsiang.
Ting Wei-fen.
Kung Hsiang-hsi (H. H. Kung).
Tsou Lu.
Chen Li-fu.
Yeh Chu-tsang (secretary-general).

Central Political Council—

Wang Ching-wei (chairman).
Chiang Kai-shek (vice-chairman).
Wang Chung-hui.
Madame Wang Ching-wei.
Yen Hsi-shan
T. V. Soong.
Chang Hsueh-liang (the ''Young Marshal '').
Ho Ying-chin, and seventeen others.

Executive Yuan-

President: Chiang Kai-shek. Vice-president: H. H. Kung.

Legislative Yuan-

President: Sun Fo. Vice-president: Yeh Chu-tsang.

Judicial Yuan-

President: Chü Cheng. Vice-president: Tan Chen.

Examination Yuan-

President: Tai Chi-tao. Vice-president: Niu Yung-chien.

Control Yuan-

President: Yü Yu-jen. Vice-president: Hsü Chung-chih.

Cabinet-

Minister of Finance: H. H. Kung.
Minister of Interior: Chiang Tso-pin.
Minister for Foreign Affairs: Chang Chun.
Minister of War: Ho Ying-chin.
Minister of Education: Wang Shih-chieh.
Minister of Industries: Wu Ting-chang.
Minister of Railways: Chang Chia-ao.
Minister of Navy: Chen Shao-kuan.
Minister of Communications: Ku Meng-yu (did not assume office).
Chairman of Mongolian and Tibetan Affairs Committee: Huang
Mu-sung.
Chairman of Overseas Chinese Affairs Commission: Chen Shu-jen.
Chairman of National Health Administration: J. Heng Liu.
Secretary-General of the Executive Yuan: Weng Wen-hao.

- 5. It speaks well for the stability of the Central Government and party organisation that twelve months later it is only necessary to make two changes in the foregoing lists: Mr. Hu Han-min has died, and General Huang Mu-sung has been transferred to another post and replaced by General Wu Chung-hsin, formerly chairman of the Kweichow Provincial Government.
- 6. There were few developments of interest in the internal political situation during the earlier part of the year. Relations between Nanking and the South-West remained as unsatisfactory as ever. The efforts which were made to conciliate the South-Western leaders and to bring them into a common front on the Japanese question at the time of the Fifth National Congress of Kuomintang Delegates were described in the annual report for 1935. Mr. Hu Han-min, who was then in Europe, was appointed chairman of the Standing Committee of the Central Executive Committee, and it was hoped that his suspicions regarding the orthodoxy of the Nanking régime's attitude towards Japan had been set at rest, and that he would consent to throw in his lot with the Central Government. He was at length induced to return to China, and every means was taken by the

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Central Government to do him honour and flatter his feelings. But he was not to be placated. He arrived in Hong Kong on the 19th January, but instead of continuing his journey to Nanking he went to Canton. Though he pleaded indisposition as his excuse for not going north, he made it plain in various statements that he was still not satisfied with Nanking's attitude to public affairs. Thus his return to China, instead of easing the relations between Nanking and Canton, had the opposite effect by focusing and setting the seal upon the hostility of the South-Western leaders to General Chiang Kai-shek and all his works.

- 7. In May the Japanese garrison in North China was augmented. The South-Western leaders seized upon this incident, and used it both as a fresh rallying point for anti-Japanese sentiment and as a stick with which to beat Nanking. Their minds had for some time been running strongly on the question of giving a lead to the rest of the country in opposition to Japanese encroachment, though the encroachment which they had in mind at that time was nearer home than North China. They had persuaded themselves that the Japanese were fomenting trouble in Fukien, with a view to creating yet another autonomous State there. In an interview with the Commander-in-chief, China Station, on the 31st March, General Li Tsung-jen stated that, if an autonomous State was started in Fukien, the South-West would at once move troops to suppress it; if Japan intervened and the South-West had to fight, the hands of the Central Government would be forced. It would either have to rally the whole country to the aid of the South-West or it would find itself abandoned; then it would fall and be superseded by stronger leaders.
- Hu Han-min, whose illness was proved to be more genuine than was generally supposed, died in Canton on the 12th May. The South-Western civilian party was left leaderless and the military element took control of the situation. On the 28th May the South-West Executive Committee issued a declaration denouncing the increase of the Japanese garrison as a violation of China's sovereignty, and calling on all Chinese to oppose this act of aggression. On the 2nd June the South-West Executive Committee and the South-West Political Council jointly despatched a telegram to Nanking urging the Central Government to give a lead to the nation in a practical policy of armed resistance. On the 5th June a joint meeting of the South-West Central Executive Committee and Political Council adopted a resolution that the First and Fourth Group Armies (the Kwangtung and Kwangsi troops respectively) be renamed the "Chinese Revolutionary Anti-Japanese National Salvation Army," and that preparations be made for mobilisation against the Japanese. In spite, however, of the fact that no order for actual mobilisation or the launching of any expedition had been given, Kwangsi troops were already advancing northwards into Hunan. On the 7th June the three military leaders of the South-West, Chen Chi-tang of Kwangtung and Li Tsung-jen and Pai Chung-hsi of Kwangsi, sent a circular telegram to all military commanders in China urging them to rise up and fight Japan.
- 9. The question at once arose whether these political and military moves were to be taken at their face value. Were the South-Western leaders seriously trying to rally the whole country to their aid in a genuine nation-wide revolt against the Japanese incubus and force the Nanking Government into the position where they would either have to join in the movement or yield place to stronger leaders (as foreseen by General Li Tsung-jen); or were their designs purely selfish and ambitious; and, so far as the two Kwangsi leaders are concerned, were they actuated solely by their ten-year-old feud with General Chiang? It was hardly possible to disentangle the truth from the welter of conflicting evidence. On the one hand it was pointed out that if the alleged anti-Japanese character of the movement was a pure bluff, it was bluff of a very dangerous kind, since anti-Japanese feelings were being roused which might easily bring the South-West into serious conflict with the Japanese; on the other hand there were indications that the Japanese not only did not take the threat to themselves seriously, but were actually in touch with the Kwangsi leaders and supplying them with funds and munitions. To those familiar with the Orient there would be nothing improbable in the Japanese supplying the South-West with help to conduct an anti-Japanese campaign. The Kwangsi leaders might well intend to fight the Japanese in North China—if they ever got so far—and borrow arms and money from Japan

for that purpose; Japan might willingly supply Kwangsi with the arms and money, knowing full well that it would be against Nanking that they would have to be used.

- Whatever their motives may have been, the appeal of the Southern leaders to their fellow militarists was greeted with such a chorus of disapproval from all parts of the country as must have startled them considerably. Not only did the other military leaders not rally to their support, but serious divisions arose in their own ranks. The Central Government were in a difficult position, but they escaped from it cleverly. On the 8th June General Chiang Kai-shek announced that, since under the resolutions of the National Congress of Kuomintang Delegates held last year (to which the South-Western delegates had subscribed) questions of peace or war could only be decided by a plenary session of the Central Executive Committee, immediate steps would be taken to summon a plenary session, and he earnestly besought the Southern leaders to observe the constitutional position, to cancel the measures already taken, and to withdraw their forces from Hunan. At the same time, to reinforce this appeal, Central Government forces were poured into the province, and though General Chiang declared that they would not fire the first shot, he also made it exceedingly plain to the South-Western leaders that they were not to be allowed to parade their forces over territory under the effective control of the Central Government. Faced with this situation the South-Western leaders had no option but to withdraw their forces and to await the result of the plenary session, which had been summoned for the 10th July. The month's interval gave time for the usual haggling behind the scenes, and it was hoped that a settlement would be reached in time for an agreed solution to be presented to the plenary session for acceptance. The Southern leaders attempted to bluff, but from the moment when it had become clear where their leadership was taking the South-West, defections both among the civilian members of the Government and in the Kwangtung fighting forces increased at an alarming rate. The dissatisfaction of the South-West with their leaders had also other grounds, the most serious of which was the mishandling of the currency situation, which had resulted in a serious economic paralysis. Suffice to say that a turn-over among the Kwangtung military leaders in favour of the Central Government occurred such as put any effective united military opposition out of the question.
- The plenary session met on the 10th July. It was attended only by five minor delegates of the South-West authorities, who were entrusted with a proposal that diplomatic relations with Japan should be severed and all humiliating Sino-Japanese agreements repudiated. The South-Western members of the Central Executive Committee and Central Supervisory Committee attended in force and rallied to the support of the Central Government against their own military leaders. The plenary session lasted only five days. In that time it-

(1) Abolished the South-West Executive Committee and the South-West Political Council

(2) Dismissed General Chen Chi-tang from the posts of Commander-in-chief of the Kwangtung forces and Pacification Commissioner at Canton, and in his place appointed as Pacification Commissioner for Kwangtung Province General Yu Han-mou, Commander of the Ist Kwangtung Army (who was one of those who had transferred his allegiance to Nanking).

(3) Appointed General Li Tsung-jen as Pacification Commissioner for Kwangsi and General Pai Chung-hsi as Deputy Pacification Commissioner (Li Tsung-jen formerly held the post of Director of the Office of Nanking Pacification Commissioner, so that his new appointment amounted to nominal promotion).

(4) Renewed the appointments of Mr. Lin Yun-kai and General Huang

Hsü-chu as Governors of Kwangtung and Kwangsi respectively.

(5) Established a National Defence Commission of eighteen members, including Generals Chen Chi-tang, Li Tsung-jen and Pai Chung-hsi.

(6) Rejected a proposal to launch an anti-Japanese expedition.

12. In explaining the rejection of the motion for the launching of an anti-Japanese expedition General Chiang restated the Government's foreign policy with somewhat more plainness than had been done hitherto. After referring to

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the resolution passed by the Fifth National Congress in November last year, in which it was laid down that: "While there is still hope for peace, we shall not abandon peace, nor shall we talk lightly of sacrifice until we are driven to the last extremity," Chiang Kai-shek went on to lay down the minimum limit to be adopted in the diplomatic policy of the Central authorities as meaning the preservation of China's territorial integrity and sovereign rights, and stated that if any one should force China to enter into an agreement for the recognition of Manchukuo and derogatory to China's territorial and sovereign rights, that would be the limit of her patience and the time for final sacrifice.

- 13. Why the resolutions of the plenary session made a distinction between General Chen Chi-tang of Kwangtung (who was removed from his post) and Generals Li Tsung-jen and Pai Chung-hsi of Kwangsi (who were confirmed in their posts and even given titular promotion) is not clear, but the plan was possibly first to shake down Chen, who was clearly tottering, and to deal with Li and Pai at leisure; once Kwangsi was isolated their position would be untenable.
- Chen Chi-tang's first reaction was to put up a bold front, and reports from Canton announced that in conjunction with the Kwangsi leaders he was about to declare the complete independence of the South-West. He soon came to realise, however, that resistance was hopeless. The whole of his air force and half his army had by now gone over to the Central Government, and he could find little sympathy or support anywhere. He accordingly threw in his hand, and on the 18th July left for Hong Kong. The Kwangsi leaders were naturally disconcerted at the turn of events. It seemed for a brief moment that there was to be a race for Canton between them and the Kwangtung (now Central Government) forces under General Yu Han-mou, which were returning to the provincial capital with all speed. Central Government troops had, however, in the meantime been pouring from Szechuen into Kweichow, thus threatening the rear of the Kwangsi forces, and the intention-if there had, indeed, been any-of challenging the Central Government for the control of Kwangtung was quickly abandoned. General Yu Han-mou re-entered Canton on the 23rd July, danger of disorder was at an end and confidence was quickly restored. The Kwangsi leaders now informed the Central Government that they were prepared to obey the decision of the plenary session, and would accept at the hands of the Central Government the posts which they were actually holding, of Pacification Commissioner and Deputy Pacification Commissioner respectively of Kwangsi. This was a somewhat embarrassing decision for the Central Government which would undoubtedly have preferred that these two generals should follow the example of General Chen Chi-tang and leave the country. The Central Government then attempted other means of dislodging these officials; General Li Tsung-jen's removal from the post of Pacification Commissioner of Kwangsi and his appointment to membership of the Standing Committee of the Military Affairs Commission were announced, and General Pai Chung-hsi was likewise relieved of his post and appointed chairman of Chekiang (in which position he not only would have no military command, but would be directly under the thumb of the generalissimo); while the Governor of Chekiang, General Huang Shao-hsiung, a trusted henchman of the generalissimo's, was appointed Pacification Commissioner of Kwangsi.
- 15. The Kwangsi leaders were unwilling to accept these terms which would have severed their connexion with the province, which they regarded almost as a feudal fief, and they prepared to defend their position by force. Rather than resort to force, and bring upon China the shame of waging a civil war while the Japanese were at her very gates, the generalissimo temporised. General Li Tsungjen was formally reinstated as Pacification Commissioner for Kwangsi, while General Pai Chung-hsi was permitted to remain in the province, though without any territorial post. He was appointed a member of the Standing Committee of the Military Affairs Commission in the hope that he would swallow the bait and come to Nanking, where he could be kept out of mischief; but though he did take the bait and allowed himself to be inducted into office on the 16th September (it being necessary for Commissioners of the Central Government to proceed to Kwangsi for the purpose), he could not be drawn from his lair, where he still remains, implacable, unyielding, a thorn in the Government's side.
- 16. While the Central Government has not been able completely to break the power of the Kwangsi generals, it has nevertheless succeeded in asserting a

considerable degree of authority in the financial, political and even military organisation of the province, and has made it clear that it could, if it would, bring the generals to their knees. Forbearance in the circumstances was a sign of strength and not of weakness in the Central Government, and General Chiang Kai-shek's settlement of the Kwangsi revolt on these terms, without bloodshed, was hailed by his fellow-countrymen as one of the greatest triumphs of his career.

- 17. Meanwhile, the Central Government has been proceeding with the reorganisation of Kwangtung and its incorporation into the National Government system. This is no easy task in view of the corruption of the administration and the jealous hostility to the new régime of the local officials. The generalissimo, who paid a visit to Canton early in September to lend the support of his own personality to the reforms, read the local officials a stern warning against corruption, which was emphasised by the execution of Dr. Feng Jui, head of the Bureau of Agriculture and Forestry, on a charge of embezzlement.
- 18. The generalissimo returned to Nanking on the 5th October, and within the next few weeks visited Hangchow, Loyang, Sian, Taiyuan and Tsinan, where he received, and held conferences with, all the leading provincial officials and military commanders in Central and North China, with the exception of General Sung Che-yuan, whom it was deemed impolitic for him to meet. The obvious inference from these activities, coinciding as they did with the failure of the Sino-Japanese negotiations at Nanking and the recrudescence of trouble in the North, was that preparations were being made for armed resistance in the event of Japan resorting to forceful measures to gain her ends.
- 19. There had for some time been indications that trouble was brewing again in Inner Mongolia. Since the eviction by the Japanese of General Sung Che-yuan's troops from North Chahar in the summer of 1935, the province has become to all intents and purposes a Japanese protectorate. Prince Teh, though he accepted from the Central Government an appointment as president of the Mongolian Local Autonomy Political Council and has been in receipt of a monthly subsidy of 30,000 dollars from Nanking, is entirely in the hands of the Japanese, and effective authority at Chapsor has, in fact, been shared by him with a Japanese military mission composed of six officers of the Kwantung Army. It was known in August that some 10,000 Mongolian troops from Manchukuo and from the Silingol Leagues were being drilled by Japanese instructors, and that active preparations were being made for an attack on Suiyuan Province, where Japanese military missions—which had, uninvited, established themselves at Kweihwa, Paotou, Pailingmiao and elsewhere—had by methods now familiar succeeded in preparing the ground. It seemed that the Japanese were taking advantage of General Chiang Kai-shek's preoccupation with the South-West to make another step towards the elimination of Chinese control from Inner Mongolia.
- 20. A skirmish took place early in August in the vicinity of Taolin between the Suiyuan troops on one side and a mixed force of Manchu and Mongol troops and irregulars on the other. The latter were repulsed and withdrew to Shangtu (West Chahar). Thereafter there was a period of tranquillity, which continued for such time as it was possible to take a hopeful view of the diplomatic conversations in Nanking; but as soon as these began to flag the Japanese puppets in Mongolia began to move again. (The rhythm of military activity in the North seems to bear some relation to the course of diplomatic negotiations in Nanking.) On the 15th November an attack by Manchu-Mongol troops and irregulars was made in the direction of Taolin, and was followed by other attacks during the following days. Though these attacks were supported by artillery and aircraft they seem to have been somewhat desultory and completely ineffective. Once again the Japanese denied that they were concerned: the fighting was, a spokesman of the Japanese Foreign Office said, a purely Chinese domestic affair, though the Japanese Government was naturally sympathetic towards any movement of the Mongols "in defence against the Communists."
- 21. The news of the renewal of hostilities produced an immediate stiffening in the Chinese attitude. The Minister for Foreign Affairs announced that his conversations with the Japanese Ambassador would be suspended so long as the existing situation continued, and I was informed confidentially that General

Chiang Kai-shek intended not only to oppose the attack on Suiyuan but to deal once and for all with the interlopers, extending the operations if necessary to Chahar and using all the resources of the Central Government for the purpose.

- 22. Central Government troops were, in fact, moved into Suiyuan. Pailingmiao, in the north of the province, where the irregulars had established themselves in some strength, was retaken without serious difficulty, and the invaders chased over the border into Chahar. But when, in the process, the Chinese forces crossed the provincial border, General Fu Tso-yi immediately received a vigorous protest from the Kwantung Army, which alleged that at the time of General Sung's withdrawal in 1935 (see paragraph 19 above) an agreement had been made between him and General Doihara that henceforth no Chinese forces should enter the Province of Chahar north of the Wall. When informing His Majesty's Ambassador of this fact, the Vice-Minister for Foreign Affairs said that the Central Government had no official knowledge of any such agreement and were considering ignoring it. Some leading members of the Government were, he said, advocating making an announcement that the Central Government refused to recognise any pacts or agreements alleged to have been made with any Chinese authorities not authorised for that purpose. The matter was still under consideration, and the Government realised that the issue was an exceedingly grave one since, if such an announcement was made and acted upon, there was serious danger of a direct conflict with the Japanese. Asked if the announcement would cover the Tangku Truce and the Ho-Umetsu Agreement, the Vice-Minister replied that these would not be affected, since they were entered into by authorised representatives of the Central Government.
- 23. The Suiyuan crisis, serious as it seemed, was at this moment eclipsed by a crisis even more serious. The old North-Eastern armies under the command of General Chang Hsueh-liang (the "Young Marshal") had for some time past been stationed in Kansu and Shensi, nominally engaged in fighting the Communist forces which had concentrated in that area. It was well known that little serious fighting had taken place, and it was reported that some at least of the Young Marshal's Communist Suppression Forces were fraternising with the Communists. The matter had caused the Government acute anxiety, and one of the reasons for General Chiang Kai-shek's visits to Sian was his desire to deal with this dangerous situation. On the 12th December the generalissimo and nearly twenty other high Government officials who were in Sian were arrested by the Young Marshal, who immediately broadcast a message to the effect that he had "requested" the generalissimo to remain in Sian for the time being and had drafted eight points of policy—the inference being that the generalissimo would not be released until he accepted the eight points. Owing to a rigid censorship, no authentic version of the eight points is procurable, but it is generally agreed that they comprised: reorganisation of the Nanking Government so as to include all parties (including the Communists); end of civil war (anti-Communist operations being included in this term) and active resistance against Japan; release of all political prisoners; safeguarding of the rights of free speech, publication and assembly; and immediate convention of a National Salvation Conference. The Central Government and, indeed, the whole country were thrown into consternation; the situation seemed to call for the most drastic measures, but drastic measures might well result in the murder of the generalissimo. Nevertheless, drastic measures were decided upon. Chang was proclaimed a traitor and a punitive expedition was ordered and actually despatched. Simultaneously, however, and apparently independently of the Government, the Soong family (including Mme. Chiang and T. V. Soong) entered into pourparlers with the Young Marshal, who was also assailed by such a chorus of denunciation from every quarter as must have surprised him considerably. At all events, his confidence was so badly shaken that on the thirteenth day after his coup he not only released his prisoner but accompanied him to Nanking and threw himself on the mercy of the Government. A military tribunal was set up to try him and he was sentenced to ten years' imprisonment. This was, however, merely a gesture intended to assert the authority of the Central Government and it was followed almost immediately by a free pardon. A plenary session of the Central Executive Committee was summoned for the 15th February to consider the political issues involved.

- 24. At the time of writing it is still difficult to disentangle either the facts or the motives of this strange episode. It has been suggested that General Chang's coup, though possibly ill-advised, was actuated by purely patriotic and disinterested motives, that he was honestly convinced that the generalissimo had fallen under the influence of pro-Japanese elements in the Government which were allowing the country to be eaten piecemeal by Japan, and that he was rendering a signal service to the State by bringing these facts home to the generalissimo. Such an interpretation cannot, however, be reconciled with all the known facts. These north-eastern troops from Manchuria had never been happy in their new quarters; there were difficulties about pay, they did not like the task of fighting so-called Communists and they felt they were not being fairly treated. Chiang, who has a difficult temper, would listen to no complaints, but embarked on the dangerous task of transferring the disaffected forces to another area and putting in others on whom he could rely. On the very day on which the coup took place the appointment by the generalissimo of General Chiang Ting-wen (who had been brought up from Fukien for the purpose) to take over command of the anti-Communist campaign was announced in Sian. It seems hardly necessary to seek further for a motive, but over-simplification would be misleading, since other influences were at work. The Government's policy of moderation and conciliation towards Japan was by no means universally popular and for some time past an extremist party, known as the National Salvation Association, had been growing in influence. Its avowed object was to make a common front of all parties in the State, including the Communists, and to take vigorous action against the Japanese encroachments in the north. The Government had found it necessary, in pursuance of its own policy, to repress the more exuberant manifestations of the extremists, and had in consequence laid itself open to the charge of pandering to the Japanese by suppression of the patriots. The similarity of the Young Marshal's eight points to the programme of the extremists would make it appear that he had come under the influence of the latter, though it may be that, as in the case of the south-west, self-interest merely disguised itself in the ready-tohand garb of patriotism.
- 25. The return of the generalissimo and the trial of the Young Marshal are, of course, not the end of the story. The anti-Communist campaign has been suspended and the Communists seem free to occupy, if they wish, the whole of Kansu. This is a situation which cannot continue indefinitely, but how the Communists and the insubordinate Communist Suppression Forces are to be dealt with is a question to which the answer is not at present obvious.
- In North China the situation at the beginning of the year was that two separate organisations were functioning independently of each other; the Hopei-Chahar Political Affairs Council, which the Central Government had set up as an expedient to stave off the Japanese pressure for a five-province autonomous zone, and the "East Hopei Anti-Communist Autonomous Council" (later transformed into a "Government") which was the Kwantung Army's counterblast. This anomalous situation has continued throughout the year and repeated attempts to bring about the dissolution of the "puppet" organisation have broken down in face of the Kwantung Army's determination to establish in the north a régime completely independent of Nanking. The price the army asks for the dissolution of the East Hopei "Government" is, indeed, the virtual autonomy of North China. It is difficult to describe or even to understand the political and economic structure of the East Hopei organisation. Without any force of its own, and unwelcome to the inhabitants of the area over which it holds sway, it exists, with its capital only a day's walk from Peking, solely by virtue of the silent menace of Japanese force. It constitutes a breach in China's military and economic line of defence by which she is robbed of all possibility of self protection, and by which her very existence is threatened. Through this breach poured out millions of silver dollars whose value was enhanced by the embargo on the export of silver imposed elsewhere in China; and through this breach continued to pour in tens of millions of dollars worth of artificial silk, cotton piece-goods and other articles, an organised traffic in smuggling which not only causes immense loss to the Chinese customs revenues, but, in certain lines, drives the honest trader out of business. This smuggling trade has now become systematised. Though the Chinese customs have not been forbidden to function in the East Hopei zone their control of the import and export trade has been neutralised by their inability to use force against the Japanese and

Korean smugglers. The latter, operating in large gangs, and armed with clubs and stones, defy any attempts to seize their goods or collect duty. All this has gone on under the complacent eyes of the Autonomous Government, who have introduced a further complication by themselves taxing the smuggled goods at approximately a quarter of the customs duty rates, while their Japanese military protectors deny the right of the customs to interfere subsequently with cargo so taxed.

- 27. The Hopei-Chahar Political Affairs Council has appeared to be becoming, under Japanese pressure, increasingly independent of Nanking. This is particularly noticeable in the financial sphere. Orders were actually issued by the council's Financial Department to the Customs, Salt and Postal Commissioners within the area controlled by the council to pay over all future revenues to the council instead of remitting them to the Central Government. The orders were ignored by the Customs and Posts, while the position of the salt revenues, which had all along been anomalous, was not seriously affected. Even before the Hopei-Chahar Council came into existence the Central Government had paid over to the Peiping Branch Military Council the bulk of the revenues from the Changlu (Hopei) salt fields after deduction of the provincial quota for the foreign loan obligations secured on the Salt Gabelle, and this arrangement has since been varied only in detail. The degree of the detachment of North China from the Central Government at any moment is, in fact, in direct relation to the degree of pressure which the Japanese are exerting, and were the internal preoccupations of the Japanese to distract their attention from North China for a space of some months they might well find all their work undone. Nevertheless, the work of separation has gone far. The position as it stands at the moment, and so far as it is ascertainable, is approximately as follows: in the political, social and economic fields the Hopei-Chahar Council is given by mandate of the Central Government, and actually enjoys a high degree of autonomy except in relation to foreign affairs. As regards foreign affairs the situation is not clear. The intention of the Central Government was to keep the control of foreign affairs in its own hands as far as possible, and by its mandate it authorised the Hopei-Chahar Council to set up a Foreign Relations Committee to discuss foreign affairs questions; the committee (which calls itself a "commission"), however, notified the foreign Embassies and Legations that it would deal with all foreign affairs questions arising within the council's sphere; but the Minister for Foreign Affairs of the Central Government, on being asked by the foreign representatives for a ruling as to the validity of this announcement, replied that the Foreign Relations Committee of the Hopei-Chahar Council was merely a research organ and had no authority to deal with diplomatic issues. The Peking-Shanhaikuan Railway has been definitely removed from the control of the Ministry of Railways at Nanking and placed under the control of the Communications Commission of the Hopei-Chahar Council, which in turn pays 100,000 dollars a month to the East Hopei Government to free the line (so far as it runs through that Government's area) and its revenues from molestation. The Customs, Posts and Salt Gabelle continue to function as Central Government organisations, though some of the personnel has had to make place for the council's nominees, and the council disposes of almost the whole of the Central Government revenues collected in its area except the customs. There are also indications that a currency separate from Nanking's will be introduced in North China, the bank notes of the China South Seas Bank, which has close relations with the Japanese, being made legal tender, but this project has not yet reached the stage of concrete achievement. (Japanese economic penetration in North China is dealt with in paragraph 158.)
- 28. One of the most important tasks facing the Central Government at the beginning of the year was the preparation for the transition from the "tutelage" stage to the "constitutional stage" of Dr. Sun Yat-sen's system of government. It may be convenient to recall that in December 1932 the then Central Executive Committee had decided that the time was approaching when the nation could dispense with the leading strings of Kuomintang party control, and that the drafting of the Constitution of the Republic should accordingly be put in hand and the National People's Congress, prescribed by Dr. Sun, convoked to adopt it and to inaugurate the period of democratic government. A draft constitution was subsequently drawn up by the Legislative Yuan and after various revisions was submitted to the last plenary session of the Fourth Central Executive Committee in November 1935. This session resolved that the draft be forwarded to the Fifth

National Congress (which was then coming into being) with a request that the latter fix an early date for the official publication of the Constitution and the convocation of the National People's Congress. The Fifth National Congress on the 4th December, 1935, resolved that the draft Constitution should be further revised, that the final draft should be published on the 5th May, 1936, and that the National People's Congress should be convened on the 12th November. The final draft Constitution was duly promulgated on the 5th May and the election of delegates for the People's Congress was at once put in hand and was pursued even in face of the great difficulties caused by the South-Western coup d'Etat; but when it became clear in the autumn that Sino-Japanese relations were once again taking a serious turn the convocation of the congress was postponed indefinitely. The excuse was made that it was found impossible to complete the elections in time, but the true reason was the realisation that it was clearly impossible to make a radical change in the system of government while faced with an international crisis of the first magnitude.

- 29. According to law the President of the National Government should hold office for two years and may be reappointed for another term of two years. In November 1935 President Lin Sen was just completing his fourth year of office. Since, however, it had been decided to convene the People's Congress on the 12th November, 1936, it was resolved that, in order to avoid unnecessary changes, President Lin Sen's term of office should be extended until the day of the inauguration of the President of the Republic after the convocation of the People's Congress. One result of the postponement of the People's Congress is accordingly the continuation in office of Mr. Lin Sen.
- 30. A feature of the Chinese internal situation which should not be passed over without some remark is the revival of Chinese national morale and self-confidence after the depression of the preceding years. It must be said that this revival is almost entirely the work of the generalissimo, who is rapidly establishing for himself a position of authority, based on the affection and trust of his fellow countrymen, such as has been occupied by no Chinese in modern times. His fiftieth birthday, which fell in October, was made the occasion of the presentation to him of some seventy fighting aeroplanes purchased by public subscription and accepted by him on behalf of the State. It is generally realised now that the generalissimo's apparent inaction in front of present humiliations in reality covers a patient activity in the task of re-educating the nation and restoring its moral, physical and material health for the single purpose of enabling it one day in the not too distant future to turn the tables on its present tormentor. It is, indeed, by no means unlikely that Japan may come to regret that she goaded a peaceful neighbour into militarism.

(2) Mongolia.

- 31. The year 1936 has seen, as regards Outer Mongolia, a more explicit declaration of its subordination to Soviet Russia (in the shape of the Soviet-Outer Mongolia Pact of Mutual Assistance) than had previously been acknowledged, and as regards Inner Mongolia, a contest between the Chinese on the one hand and the Mongolians, led by Prince Teh and backed by the Kuantung army, on the other, with the result that Japanese influence at the close of the year became established in Chahar, north of the outermost Great Wall, and Inner Mongolian Suiyuan came more effectively under the control of the Chinese authorities.
- 32. On the Outer Mongolia–Manchukuo frontier a series of serious incidents occurred on the 14th and 15th January at Olanhottok (57° 40′ N. latitude and 117° 14′ E. longitude) and at Helmut near Buir Nor, and a further clash took place at Bulun Dersun near the former place on the 12th February. These were followed by a succession of further incidents at Halhamiao and other places about the end of March, the last occurring on the 31st March and the 1st April.
- 33. M. Stalin gave an interview on the 4th March to Mr. Roy Howard of the World Telegram, openly declaring the absolute support of Outer Mongolia by the Union of Soviet Socialist Republics against serious military attack by Japan, and this was followed by the conclusion of the Soviet-Outer Mongolian

Pact of Mutual Assistance at Urga on the 12th March, articles 1 and 2 of which provided as follows:—

Article 1.—In the event of the menace of an attack upon the territory of the Union of Soviet Socialist Republics, or upon that of the "Mongolian People's Republic," on the part of a third State, the Governments of the Union of Soviet Socialist Republics and of the "Mongolian People's Republic" shall undertake immediately to consider jointly the situation that has arisen, and shall take all measures necessary for the protection and security of their territories.

Article 2.—The Governments of the Union of Soviet Socialist Republics and of the "Mongolian People's Republic" undertake in the event of a military attack upon one of the contracting parties to render each other every assistance, including military assistance.

- 34. A copy of this pact was communicated to the Chinese Government on the 2nd April in answer to enquiries made as to the existence of such a scheme, and subsequently a protest was made by the Chinese Government to the Soviet Government, and replied to by the latter, after which a further protest was made by the Chinese Government and the matter then dropped. One result of the conclusion of the pact has been the complete cessation of incidents on the Outer Mongolia–Manchukuo frontier, the last being that of the 31st March—1st April referred to in paragraph 32 above.
- 35. Negotiations between Outer Mongolia and Manchukuo were resumed in the spring and progressed slowly, and on the 28th August it was announced that the conference broken off in November 1935 would be resumed at Manchuli on the 25th September (later postponed to the 1st October). The conference, however, hung fire, and after the formal opening session on the 15th October little headway was made and no concrete results appear to have been achieved.
- 36. As regards Inner Mongolia, the Nanking Government, in an effort to save something of the situation (referred to in paragraph 15 of 1935 annual report) by playing off the Suiyuan Mongols against the Chahar Mongols led by Prince Teh, created in January 1936 the Suiyuan Inner Mongolia Local Autonomy Political Affairs Council with jurisdiction over the Mongolian Leagues and Banners in Suiyuan, including the Ulan Tsab and Ordos Leagues, the Tumet Banner near Kweihua, and the four Right Wing Chahars in the five hsiens of East Suiyuan.
- 37. The Chahar Mongols led by Prince Teh were strongly dissatisfied with this step as constituting an obstacle to the realisation of their dreams of a Greater Mongolia, and in May and June rumours were current as to the forthcoming establishment of a new independent Mongolian Government with headquarters at Chapsor. No such proclamation took place, however, but about this time the Japanese, already in virtual control of the six hsiens in Chahar north of the outermost Great Wall, set up a dominating position over Prince Teh, now head of the Silingol League, and established Japanese military missions at Prince Teh's headquarters and other places in Inner Mongolia.
- 38. Subsequent to the creation of the Suiyuan Mongolian Council referred to above, the Nanking Government in July reorganised the original Pailingmiao Mongolian Council (which was created in 1934) as the Chahar Inner Mongolia Local Autonomy Political Affairs Council with headquarters at Chapsor and appointed Prince Teh chairman. This appointment, together with the continuance of a subsidy from Nanking, Prince Teh accepted, although now entirely under the thumb of the Japanese; in fact, he has up to the end of the year maintained his connexion with the Chinese Central Government, and according to published telegrams sent out by him his only quarrel is with the Suiyuan provincial authorities.
- 39. In the middle of August skirmishing took place at Taolin in Suiyuan near the Chahar border between Manchukuo-Mongolian forces and the Suiyuan troops, but the attack was repulsed by the latter. An uneasy truce prevailed for some weeks until the middle of November. On the 10th November the Waichiaopu requested the immediate evacuation of all foreigners from the Provinces of Suiyuan, Ninghsia, Chinghai, and Inner Mongolia generally. The first attack

was made on the 15th November at Taolin, and thereafter hostilities developed on the Chahar-Suiyuan border between Prince Teh and two other Mongolian-Chinese leaders inspired and directed by the Japanese authorities on the one hand, and the Suiyuan provincial troops, supported by the Central Government forces and aircraft, on the other. These hostilities resulted in the capture by the Suiyuan troops of Pailingmiao on the 24th November, and of Tamiao (Sharamuren) about the 10th December. With the occurrence of the Sian incident another lull supervened which, by the end of the year, had not been broken.

(3) Sinkiang.

- 40. The position at the beginning of the year was that the Chinese Provincial Government, headed by Sheng Shih-tsai, in Urumchi, were in effective control of the whole province with the exception of the Khotan area occupied by the Tungans in the south. Negotiations between the Provincial Government and the Tungans which had been in progress intermittently for many months were brought to a successful conclusion in April. The actual terms of settlement are not known but it is reported that the Tungans finally agreed to be content with retaining military control in Khotan, the troops being paid by Urumchi, while the civil administration would be conducted by the Provincial Government. Peace reigns again in the oases.
- In the spring there were reports, principally from Japanese sources, that the Soviet Government had signed a treaty with the Provincial Government for the specific purpose of preventing the intervention of any third Power in the economic, military and political affairs of the province. The treaty was alleged to provide for the employment of five Soviet experts to serve on various committees, for co-operation in resistance to invasion, for the supply by the Soviet Government of materials for reconstruction in Sinkiang, for noninterference by the Soviet Government with the sovereign rights of Sinkiang, for Soviet assistance, political, military and economic, in case the Sinkiang Government should make any advance towards Manchukuo or Inner Mongolia, and for the concession to the Soviet Government of the right to construct a railway from Tihua to Suiyuan. The authenticity of this alleged treaty has never been confirmed but in the opinion of His Majesty's consul-general at Kashgar it accords with actual conditions in the province and is not inherently improbable. The Soviet ascendancy in provincial affairs has, indeed, increased rather than diminished during the year and a steady pressure has been exerted, accompanied by systematic persecution, to eliminate all other foreign influence from the province. The pressure seems to be principally directed against the British, and it would appear, from the number and variety of the obstacles put in the way of British-Indian traders, that the Provincial Government is deliberately strangling all communication between India and Sinkiang. No such obstacles exist to traffic over the Soviet-Sinkiang frontier. His Majesty's consul-general in Kashgar described the position of himself and of British subjects generally as a "mixture of boycott and siege."
- 42. The relations between the Central Government and Urumchi remain substantially unchanged: while the Tupan and his Government profess to take their orders from Nanking, and frequently shelter themselves behind Nanking when pressed in controversy, in practice they almost invariably ignore orders from the Central Government. The officials in the Ministry for Foreign Affairs have more than once admitted that they could not even obtain replies from Urumchi to communications made on behalf of this Embassy.

(4) Tibet.

- 43. The search for the reincarnation of the Dalai Lama has proceeded in a desultory manner throughout the year, and the Government has remained in the hands of the Regent and Council.
- 44. The Panchan (Tashi) Lama's return to Tibet has continued to hang fire. At the beginning of the year he was at the monastery of Kumbum in Chinghai still haggling with the Lhassa Government regarding the status and treatment he was to receive on his return to Shigatse. The Government of India were anxious to facilitate his return, which seemed in the best interests both

of Tibet and of India, and offered the services of Mr. Gould, British Resident at Sikkim, for the purpose of effecting a compromise. The offer was, however, rejected by the Tibetan Government, who stated categorically that they did not wish His Majesty's Government's intervention in the settlement of their dispute with the Panchan Lama, since this was a matter of internal concern.

- 45. They were, on the other hand, very anxious to retain the support of His Majesty's Government vis-à-vis the Chinese Government. Mr. Gould accordingly received an invitation to visit Lhassa in the autumn to discuss this and kindred matters. He reached Lhassa in August and was still there at the end of the year. The main point on which the Tibetan Government sought the support of His Majesty's Government was that of the escort and commissioner attached by the Chinese Government to the Panchan Lama to accompany him back to Tibet. They repeatedly assured Mr. Gould that they had the strongest objection to the escort and the commissioner entering Tibet, and that they had on numerous occasions so informed the Chinese Government. Diplomatic representations were accordingly renewed by His Majesty's Ambassador at Nanking with a view to dissuading the Chinese Government from sending the escort and commissioner. The Chinese Ministry for Foreign Affairs, however, denied that they had received any protests from the Tibetan Government. Thereon, for the purpose of refuting the Chinese statement, the Tibetan Government addressed a letter to the chairman of the Mongolian and Tibetan Committee in Nanking repeating their objections, and they asked that this be transmitted through British official sources. The letter was eventually handed to a secretary of the committee by a secretary of His Majesty's Embassy, after the Vice-Minister for Foreign Affairs had refused to accept it at the hands of His Majesty's Ambassador. Further representations by His Majesty's Ambassador against the despatch of the escort and commissioner followed. Meantime the Panchan Lama, with part of the escort, had travelled from Kumbum to Yushu (Jyekundo), where he finds himself at the end of the year.
- In the summer, Communist forces, which had been moving up and down the Sikang-Szechuen border, were in the Kanze-Derge area in the north-west of Sikang, where they burned and sacked a number of monasteries and villages. They subsequently withdrew into Szechuen, and the area vacated by them was occupied by Chinese forces. These events seem to have reminded the Central Government that though these border territories had nominally been converted into a province (Sikang), no effective administration had yet been established there. General Liu Wen-hui, Commander of the XXIV Army and one of the two leading military men in Szechuen, was appointed chairman of the Sikang Administrative Commission, and set out in November with a small force of troops for Kangting, the capital of the new province. This action is regarded with natural misgiving by the Tibetans, since the territory which the Chinese propose to incorporate into Sikang includes a large portion of Inner Tibet, and a recrudescence of the dormant frontier disputes is to be anticipated.

(5) Military Operations.

47. During the year under reference, military operations in China have consisted of-

(a) Uninterrupted operations against Chinese Communist forces, whose incursion into Shansi was the most important activity, involving the use of Central Government troops in a province hitherto sacrosanct;

(b) An overwhelming concentration in June and July of Central Government troops in the Provinces of Fukien, Kiangsi, Hunan and Kweichow, designed to deal with a threat of rebellion from the South-West Provinces of Kwangtung and Kwangsi;

(c) The despatch in November of Central Government troops to assist the provincial forces of Suiyuan and Shansi in dealing with a threatened invasion of Eastern Suiyuan by a mixed force of Mongol, "Manchukuo" and bandit irregulars from Chahar; and

(d) A concentration of Central Government troops towards South Shensi, designed to deal with the situation created by General Chang Hsueh-liang, who broke out into open revolt on the 12th December, 1936.

- 48 At the end of 1935, the Communist situation was as follows:-
- (a) Liu Tze-tan and Hsu Hai-tung, who had been joined by Mao Tze-tung in November, were in the area Wuchichen-Chingtingshan, in West Central Shensi.

(b) Hsu Hsiang-chien, with whom in November Chu Teh had thrown in his lot, had moved eastwards from Yaan towards Tienchuan (both in West Szechuan).

- (c) Hsiao Ko and Ho Lung from North-West Hunan, after overrunning West Central Hunan, had arrived at Supu, near the right bank of the Yuan River in Western Hunan.
- 49. As regards the Shensi group of Communists, in the middle of February 1936, the main body, estimated at 20,000 strong, under Mao Tze-tung, Liu Tze-tan and Hsu Hai-tung, crossed the Yellow River into Shansi in the vicinity of Liulin (West Central Shansi). The provincial forces proved useless, and by the end of the month the Communists were firmly established in West Central Shansi.
- 50. Following up their success, the "Reds" pressed westwards towards the Fenchow (Fenyang) area. During the first half of March they were very active to the north and south of Fenchow, and as a result of their activities two Shansi divisions were badly handled. Shortly afterwards Lingshih, on the Tung-Pu Railway, fell into their hands, and by the end of the month Communist bands had cut the railway in several places between Lingshih and Hungtung, thereby endangering a number of British missionaries and their families stationed at Hungtung and Linfen (South-West Shansi). To deal with this situation strong representations were at once made by the Embassy to the Chinese Government at Nanking. In addition, the military attaché was despatched to Taiyuanfu, the capital of Shansi, in order to be in close touch with the Chinese military authorities.
- 51. The suddenness of the invasion and the inefficiency of the Shansi troops had caught the Nanking Government napping.
- 52. To meet the emergency six Government divisions were ordered into the province. Two divisions of the XXXIInd Army were rushed westwards along the Cheng-Tai Railway in order to safeguard Taiyuanfu. Units of the XXIXth Army, under Sung Che-yuan in Hopei, were despatched to strengthen the defences of the Hopei-Shansi border, whilst Government troops from North Honan began to pour into the south-west of Shansi.
- 53. Orders were issued for a methodical advance southwards from Kiehsui on the Tung-Pu Railway and northwards from Yungcheng (South-West Shansi), with a view to recovering the railway and driving the "Reds" westwards. One division of Government troops was sent to Changchih (South-East Shansi) in order to prevent the "Reds" from attempting to move eastwards, and thereby threatening an invasion of North Honan.
- 54. These preparations had the desired effect. The "Reds" began to move gradually westwards from the railway, and early in April Hungtung and Linfen were relieved and the threat to the missionaries removed. During the fighting Liu Tze-tan was mortally wounded.
- 55. Early in May Mao Tze-tung and Hsu Hai-tung and the main body of Communists succeeded in crossing the Yellow River in the vicinity of Shihlou and Yungho (West Central Shansi) and re-entering Shensi. According to reports they were severely handled by Government aeroplanes whilst crossing the river.
 - 56. By the middle of May Shansi Province was declared free of Communists.
- 57. From Yenchuan (North-East Shensi) the Communists spread westwards, and succeeded in again establishing themselves throughout the whole of the north of the province. To harry their movements General Chang Hsueh-liang, who was directing Communist suppression operations from Sian, the capital of Shensi, ordered the LXVIIth Army (four divisions), under Wang I-chih, to advance northwards on Fushih (North Central Shensi) in conjunction with Shensi provincial troops under Yang Hu-cheng, who was directed to advance northwards from Hancheng (East Central Shensi), with a view to linking up with four Shansi

and Nanking Government divisions that had followed the Communists across the Yellow River into North-East Shensi.

- 58. This threat of an encircling movement from the south and east caused the Communists to withdraw in a leisurely manner to the region of the Shensi-Ninghsia-Kansu borders, where they were left in peace for some months. In November they were again on the move, and by the end of that month the main body had occupied the area Haiyuan-Kuyuan in North-East Kansu, where they joined hands with Ho Lung and Hsiao Ko, the Communist leaders from North-West Hunan.
- 59. It cannot be said that any serious fighting took place during this period; in fact, by the end of November there were indications that Chang Hsueh-liang's troops and the Shansi provincial troops were fraternising with the Communists. Chang Hsueh-liang at Sian on the 12th December, 1936, broke out into open revolt, and since then no news has been received in connexion with the activities of the Communists mentioned in this paragraph.
- 60. During February and March the Communists under Hsu Hsiang-chien and Chu Teh moved northwards from Tienchuan (West Central Szechuan) and, skirting Mowkung, they eventually established themselves in the area Tanpa-Tsunghua-Suichingtun (North-West Szechuan-Sikang border). Little followed until September, when it became evident that they were again on the move with South Kansu as their objective. Failing to capture Minhsien, an important town in South Kansu, the Communists next moved on and occupied the Changhsien-Lungsi-Weiyuan area (all north-east of Minhsien). From here they proceeded north-eastwards, and during the early part of October fierce fighting was reported to have taken place astride the Sian-Lanchow highway in the vicinity of Huining and Tsingning (south-east of Lanchow). Breaking through the Government lines, the Communists moved north-westwards and succeeded in crossing the Yellow River in the vicinity of Chingyuan (north-east of Lanchow). Reports received during the latter part of December indicate that this group of Communists is now in the area Yungchang-Santan in North-West Kansu.
- 61. During January 1936 the Communist forces under Hsiao Ko and Ho Lung moved south from Supu to Suining in South-West Hunan. Pressed by provincial and Government troops, they then moved into Kweichow Province via Kuanhsien (on the Yuan River). This led to three Kwangsi divisions being despatched to Tuyun in South-East Kweichow with orders to oppose any attempt made by the Communists to move southwards towards the Kweichow-Kwangsi border.
- 62. By the end of January Kweiting, some 30 miles east of Kweiyang, had fallen into the hands of the Communists. This constituted a serious threat to the capital of the province, and in consequence martial law was proclaimed and Kwangsi troops were rushed to Lungli, east of Kweiyang.
- 63. Skirting the capital to the north, the Communists next moved via Kiensi and Tating to Pichieh on the Kweichow-Yunnan border. Attacked by Government forces they separated into two columns and moved south-westwards—one via Weining and Suanwei and the other via Suicheng and Panhsien, joining up in the vicinity of Kutsing (East Yunnan).
- 64. By the middle of April the Communists, having threatened and skirted Kunming (Yunnanfu), had crossed the Putuho (River) and captured Tsuyung (west of Yunnanfu). From Tsuyung they moved north-eastwards to Likiang, threatening Tali on the way. All missionaries had been evacuated, but considerable apprehension was felt in Tengyueh, where hurried preparations were made to withstand a siege. Fortunately the danger did not materialise and early in May the Communists had crossed the Upper Yangtze and captured Chungtien (North-West Yunnan). It was now evident that they were endeavouring to link hands with Hsu Hsiang-chien and Chu Teh on the Szechuan—Sikang border.
- 65. Government forces pushed forward via Tali to Chungtien, and this caused the Communists to move northwards towards Paan (Batang) in Sikang. They remained in occupation of North-East Sikang for some months and early in September moved along the Szechuan-Tsinghai border into South Kansu. Moving eastwards, they next threatened Hanchung (Nancheng) in South-West

Shensi, but by November they had swung north-westwards and joined up with the Communist forces under Hsu Hsiang-chien and Chu Teh in the Tsingning-Huining area.

- 66. Having taken part in the fighting that occurred in this area, Hsiao Ko and Ho Lung parted with Hsu Hsiang-chien and Chu Teh and, moving northeastwards, succeeded in joining hands with the Communists under Hsu Hai-tung and Mao Tze-tung in the Haiyuan-Kuyuan region in North-East Kansu. As far as is known there has been no change in the situation during December.
- 67. It will thus be seen that the most important Communist leaders and their forces are now concentrated in North Kansu. Had Chang Hsueh-liang and his troops in Shensi remained loyal the Nanking Government could have been well satisfied with the results of the year's anti-Communist campaign.
- 68. The Provinces of Hunan, Szechuan and Shensi had been cleared of Communist forces, and the prospects of dealing once and for all with the Communist menace appeared bright. It is true that since the outbreak of the south-west revolt in June 1936, little headway has been made in dealing with the Chinese Communists, and on the surface it might be assumed that an understanding existed between the Nanking Government and the Communist leaders. Force of circumstances may have led to vague promises and understandings, but since the collapse of the south-west revolt Marshal Chiang Kai-shek has let it be known that there was to be no compromise; and it was with a view to enforcing stricter measures against the Communists that he visited Loyang in early December. As a result of his detention by Chang Hsueh-liang everything has again been thrown into the melting pot, and at the present time it would be foolish to attempt to predict the likely course of future events.
- 69. Chang Hsueh-liang's rebellion appears to have been directed mainly towards bringing about a rapprochement between the Communist leaders and the Nanking Government. Marshal Chiang Kai-shek's outspoken remarks on the subject of communism in China would suggest he knows such a course would bring him into very serious conflict with the Japanese.
- 70. In June 1936 the semi-independent military leaders in Kwangtung and Kwangsi raised the standard of rebellion. Although it was made out to be a desire for war against Japan there is no doubt but that the plot was designed to bring about the downfall of Marshal Chiang Kai-shek and the Nanking Government.
- 71. Following the traditional line of advance from the south, the Kwangtung and Kwangsi troops crossed the southern Hunan border and penetrated as far north as Chenchow (South-East Hunan) and Yunchow (South Central Hunan). The Nanking Government accepted the challenge and an overwhelming concentration of Government troops took place in provinces immediately north of the recalcitrant area.
- 72. This affair was settled eventually by political action to the advantage of the Nanking Government, and despite hysterical press reports to the contrary, nothing more than light skirmishing took place between the advanced elements of the opposing forces.
- 73. Towards the end of 1936 considerable attention was being paid throughout the whole of China to the situation that had arisen in Eastern Suiyuan.
- 74. A large force of Mongols from Chahar and "Manchukuo" irregulars from Jehol had concentrated in the area Nanhaoyen—Shangtu (South-West Chahar) and were threatening an invasion of South-East Suiyuan. In addition, a force of Chinese renegades under a bandit leader named Wang Ying had occupied Pailingmiao, an important lamasery some 100 miles north-west of Kweisui, the capital of Suiyuan. These forces had been organised, trained and equipped by the Japanese, and were being used with the intention of obtaining control of the Ping—Sui Railway and driving Chinese influence from out of Suiyuan.
- 75. Although the Nanking Government had no desire to be drawn into a head-on conflict with the Japanese, public opinion demanded that support should

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be afforded to General Fu Tso-yi, the chairman of Suiyuan, whose provincial forces were primarily responsible for the safety of the province.

- 76. In August and again in November there had been minor clashes between the opposing forces in the vicinity of Taolin (west of Shangtu), and this led to the despatch of two Government infantry and one cavalry divisions to the scene of action.
- 77. Encouraged by the wholehearted support of the nation the Chinese forces on the 24th November staged a surprise attack on Pailingmiao, which proved entirely successful. The wireless equipment of the Japanese military mission at Pailingmiao, together with many incriminating documents that confirmed the association of the Japanese with the movement, fell into the hands of the Chinese, whilst the intruders were driven eastwards in headlong flight.
- 78. Following up their unexpected success, the Chinese next turned their attention to Sharamuren, an important cluster of temples some 60 miles to the north-east of Pailingmiao. By this time the "irregulars" had lost all stomach for fighting, and on the 11th December Sharamuren was occupied by Chinese troops without resistance. The "irregulars" in turn surrendered wholesale, and in due course were incorporated within the ranks of their erstwhile enemies.
- 79. The Chinese forces then turned their attention to Shangtu and Chapsor. Both these places are just within the Western Chahar boundary, the latter place being situated on the important Kalgan–Ulanbator (Urga) highway.
- 80. Such a move would have brought the Chinese forces within Chahar territory, and in addition would have been the first step towards reasserting the authority of the Nanking Government within that province.
- 81. During these interesting developments the Japanese played "possum," merely contenting themselves by saying that this was a domestic affair that should be dealt with by the Chinese authorities. They went on to add, however, that they would be obliged to intervene, should the situation develop in such a way as to imperil the western frontier of "Manchukuo."
- 82. Owing to Chang Hsueh-liang's coup de théâtre on the 12th December, the world was not given the opportunity of learning just when the Japanese considered the western frontier of "Manchukuo" was in danger.
- 83. This new crisis damped the spirits of the Chinese firebrands, and since then the threatened invasion of Chahar by Chinese forces has faded into the background.
- 84. From the military point of view the Chinese can congratulate themselves on three points.
- 85. They have achieved success, albeit of a minor nature, in the field; they have driven the invaders from out of Suiyuan and, finally, they have called a halt to Japanese penetration within the province.
- 86. On the 12th December, 1936, at Sian, the capital of Shensi, General Chang Hsueh-liang, Vice-Commander-in-chief of the North-West Bandit Suppression Forces, staged a remarkable coup d'Etat. He forcibly detained his immediate superior Marshal Chiang Kai-shek, together with some twenty other important military and Government officials.
- 87. Without entering into the political aspect of the situation, it is sufficient to say that the Nanking Government again accepted the challenge.
- 88. A punitive expedition was ordered against Chang Hsueh-liang with General Ho Ying-chin, Minister for War, in supreme command. General Liu Shih, Pacification Commissioner for Honan and Anhwei and General Ku Chutung, Governor of Kweichow, were appointed Commanders-in-chief of the Eastern and Western Route Armies respectively.
- 89. Loyang, on the Lung-Hai Railway, became the base of operations. The air force of the Nanking Government established itself at Loyang, whilst a heavy concentration of Government troops took place at Tungkwan, some 130 miles to the west of Loyang. General Hu Tsung-nan, commander of the 1st Nanking Government Division (at that time stationed in Eastern Kansu), was given the

rôle of preventing any attempt on the part of Chang Hsueh-liang's rebellious troops to join hands with the Chinese Communists in North-East Kansu.

- 90. From the military point of view very little happened. No serious clash occurred between the opposing forces. A railway bridge in the vicinity of Weinan was damaged by the rebels, and this led to a break in railway communications between Tungkwan and Sian.
- 91. Political forces were again brought into action, and on the 25th December Marshal Chiang Kai-shek was released and he returned to Nanking together with Chang Hsueh-liang.
- 92. On the 27th December orders were issued for the air force and troops to return to their original stations.

(6) Piracy.

- 93. No piracies of British ships occurred during the year 1936.
- 94. During the night of the 6th November, however, a Chinese vessel, the steamship Pao Hua, was pirated in the vicinity of Woosung. The victim, a vessel of about 700 tons gross, owned by the Pingan Steamship Company, of Shanghai, was outward bound for Haimen in Kiangsu on the north bank of the Yangtze, via Tsungming, with some 500 Chinese passengers on board. At about 7 P.M., after passing Woosung, the pirates, estimated at between fifteen and twenty in number, who had come on board at Shanghai in the guise of passengers, took forcible control of the ship and relieved the ship's officers and passengers of money and valuables.
- 95. The attack was well organised and most, if not all, of the pirates were armed with revolvers, the three Chinese guards having been, it is reported, overcome without a struggle. At 11 p.m. the ship, navigated under the direction of the pirates, dropped anchor off Tsungming Island and was met by a junk, obviously by previous arrangement, to which the loot was transferred. The steamship Pao Hua succeeded in returning to Shanghai under her own steam several hours later.
- 96. Towards the end of September His Majesty's consul-general at Canton was instructed to profit by the presence of General Chiang Kai-shek in Canton to take up with him the question of the suppression of piracy particularly in the Bias Bay area, and to report on the existing situation as regards the co-operation of the Kwangtung authorities with the British naval authorities in anti-piracy measures.
- 97. His Majesty's consul-general subsequently reported that General Chiang Kai-shek had stated to him that he attached great importance to the suppression of piracy, and had promised to give special instructions to the Pacification Commissioner for its complete eradication in South China.
- 98. In the middle of December His Majesty's consul-general reported that he had received from Dr. Phillip K. C. Tyau, Special Delegate for Foreign Affairs for Kwangtung and Kwangsi, a letter claiming that four out of the ten pirates who seized the steamship *Tungchow* in February 1935 (please see paragraph 73 of annual report for 1935) had been arrested and executed, while the search for the leader, Fong, was still being prosecuted.
- 99. In the course of the year discussions took place between the Commander-in-chief of the China Station and Messrs. Butterfield and Swire and Messrs. Jardine, Matheson with the object of improving the existing anti-piracy organisation. A satisfactory test was made of a new high frequency wireless attachment on board the steamship Shuntien belonging to Messrs. Butterfield and Swire, as a result of which both this firm and Messrs. Jardine, Matheson and Co. agreed to fit high frequency attachments to all their passenger ships on northern routes subject to the approval of the Admiralty for the institution of a naval anti-piracy organisation at Shanghai. This latter question is, at the time of writing, still under consideration by the Admiralty.
- 100. In September the Chinese Government acceded to the request of His Majesty's Embassy that instructions should be given to the wireless stations at Foochow, Amoy and Swatow to pass on distress messages from British ships.

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101. In May it was decided that owing to improved political conditions the military armed guards employed on British merchant vessels trading on the Yangtze should be temporarily withdrawn. In September the matter was reconsidered and the period of temporary withdrawal extended until September 1937.

(7) Banditry.

102. On the 12th April, M. Bosshardt, the Swiss missionary who was captured by the Communists at the end of 1934 (please see paragraph 85 of annual report for 1935), was released unconditionally. The reason for his release is not clear, but the Communists informed him that it was because he was a citizen of Switzerland, a country which was not imperialistic and had no concessions in China.

103. On New Year's Eve 1935 there occurred an armed robbery of the premises of the China Inland Mission at Luhsien, Szechuan. A number of armed men attacked the house and after binding the two inmates, Miss Crystall and Miss Williams, made off with everything they could find of value. The case was finally settled locally.

104. At the beginning of June M. Samset, a Norwegian subject, was kidnapped by bandits from a motor bus on the road between Hwayuan and Laohokow in the Province of Hupeh.

II.—Foreign Relations.

(A) British Empire.

(1) General

Death of His Majesty King George V.

105. The death of His Majesty King George V on the 21st January caused widespread grief throughout the country and many messages of condolence were received both by the Embassies in Nanking and Peking and by His Majesty's consular officers from officials, both Chinese and foreign, and from members of the British communities in China.

106. In Nanking on the 28th January at 11 a.m. a memorial service was held in the dining-room of His Majesty's Ambassador's house, which was attended by General Chiang Kai-shek in person and some forty other Chinese officials, by the British community and by representatives of the foreign missions. In Peking, in view of the smallness of the chapel, three memorial services were held, which were attended by the Embassy guard, the members of the Diplomatic Body and Chinese officials and the British colony respectively. The services in Peking were conducted by the Right Rev. Bishop F. L. Norris, assisted by two chaplains.

(2) United Kingdom.

(a) General.

markedly closer during 1936, and it is no exaggeration to say that they are more cordial now than they have been for many years. Many factors have contributed to this desirable end, the chief of them being the pressure of Japan and a conviction among the leaders of the Government in Nanking that Great Britain, more than any of the other Powers, is in a position to mitigate that pressure, and the very real help which His Majesty's Government in the United Kingdom have extended recently to China in her efforts to rehabilitate her economic situation. Among manifestations of a rapprochement between the United Kingdom and China have been the mission of Sir Frederick Leith-Ross, the desire of the Minister of Marine to continue the Naval Mission with an increased personnel of British naval officers, the appointment of a mission of officers of the Royal Tank Corps, the desire to appoint an Air Force Mission beginning with the appointment of Squadron Leader Malley as air adviser. The award to United Kingdom firms of the contracts for the construction of the Canton Iron and Steel Works, the Kweichi Railway and the Canton Waterworks is further evidence of a desire to improve and consolidate the relations between the two countries. If China can succeed in overcoming her internal difficulties we shall probably be

better placed than any other foreign power to take advantage of the large programme of economic reconstruction which the Chinese Government are now inaugurating. In this connexion the German-Japanese agreement against communism signed on the 25th November should operate strongly to our advantage in obtaining Chinese contracts. In an interview given to Reuter's in September General Chiang Kai-shek stated that it was his life-long ambition to promote a relationship of true and lasting friendship between Great Britain and China. Now, more than at any previous time in the history of Sino-British relations, this ambition was conditioned on circumstances entirely favourable to its fulfilment.

108. On the 5th April Sir Alexander Cadogan, His Majesty's Ambassador to China, left to take up his appointment as Deputy Permanent Under-Secretary at the Foreign Office. He was succeeded by Sir Hughe Montgomery Knatchbull-Hugessen, who arrived at Shanghai on the 14th September. Mr. R. G. Howe, counsellor of Embassy, acted as Chargé d'Affaires in the interim. Sir Hughe presented his credentials to the President of the National Government of China on the 23rd September. Sir Frederick Leith-Ross left China on the termination of his mission on the 25th June and Mr. Hall-Patch remained as economic adviser to His Majesty's Embassy. Group-Captain Willock, R.A.F. was succeeded as air attaché by Wing-Commander Kerby, D.S.C., A.F.C., on the 15th November. On the 11th December Mr. W. M. Kirkpatrick, previously Member of Parliament for Preston, left England on his appointment to China as representative on the staff of His Majesty's Ambassador of the Export Credits Guarantee Department. The commercial counsellor and financial adviser moved in to new and commodious offices in the Jardine, Matheson building on the bund in Shanghai, which were formally inaugurated by His Majesty's Ambassador on the 1st December.

109. Other items of interest in regard to British personnel not directly connected with His Majesty's Embassy were the departure on the 23rd December of Commodore Morse, R.N., on the termination of his appointment as naval adviser to the Chinese Government, the appointment of Mr. C. Rogers of the Bank of England as adviser to the Central Bank of China and the appointment of Squadron-Leader Malley as air adviser to the National Aviation Commission.

110. Shortly before he left China Sir Alexander Cadogan was asked by General Chiang Kai-shek to submit suggestions for assuring a lasting co-operation between China and Great Britain. At a subsequent interview on the 1st April Sir Alexander complied with the generalissimo's request. He observed that co-operation must be mainly in the economic field, and he handed to the generalissimo a memorandum setting out our main grievances against China in this sphere. These included disregard of contractual obligations, the most important of which were represented by the various railway agreements, disregard of contractual obligations towards banks and private lenders, discriminatory legislation, restrictions on ownership of land, establishment of monopolies, high tariffs and taxation and difficulties placed in the way of British shipping. Mme. Chiang Kai-shek undertook to draw the generalissimo's attention to the memorandum from time to time while copies were, at the latter's request, also sent to the Executive Yuan and the Ministry for Foreign Affairs for examination and action.

111. During the year settlements were arrived at of long outstanding defaults in various railway and loan agreements.

(b) British Barracks at Shanghai.

112. No further developments have taken place in connexion with the proposal put forward in 1935 that, with a view to demonstrating their continued interest in the Far East and their determination to maintain that interest, His Majesty's Government in the United Kingdom should construct new permanent barracks in Shanghai capable of accommodating strong reinforcements to the present British force. In September His Majesty's Ambassador inspected the British barracks at Shanghai and was disagreeably impressed by the poor and inadequate quality of the accommodation provided, from which the health of the troops appeared to have suffered. In 1935 the War Office called for estimates for new permanent barracks. It was learned incidentally in August last that the War Office anticipated that British regular troops would be stationed in Shanghai for several years to come.

(c) New Embassy Site.

113. The negotiations for the purchase of the site of the new Embassy at Nanking recommended by Sir Alexander Cadogan as the best available, have dragged on throughout 1936 and were still continuing by the end of the year. The price of the land and the amount of road-making charges have, however, been agreed upon and the Chinese Government have also agreed to enlarge the site by an additional 20 mow, making 100 mow in all. In June the Waichiaopu submitted drafts of the form of application for the lease and the form of perpetual lease certificate. The latter was unobjectionable, but the application form contained provisions to the effect that the Chinese Government should have the right to approve the building plans and inspect the premises during construction. It was also laid down that if His Majesty's Government desired at some future date to dispose of the land and buildings the latter should revert to the municipality or be sold only to Chinese or other foreign mission with the consent of the Chinese Government. As regards the first point, His Majesty's Government agreed to submit plans but were unable to agree to inspection during construction on the grounds of the diplomatic immunity attaching to the site once the lease had been signed. They agreed to accept the second stipulation on condition that if the Chinese Government should refuse their consent to a proposed sale of the property the municipality would take over the land and buildings at the market price, to be determined in the event of disagreement by an arbitrator. On the 29th June, the Parliamentary Under-Secretary for Foreign Affairs announced in the House of Commons that His Majesty's Government considered that the time had come to remove the British Embassy from Peking to Nanking as soon as fitting premises could be erected in the capital. In answering a subsequent parliamentary question the Secretary of State made it clear that abandonment of the Peking Embassy premises was not contemplated and pointed out that there were important British interests in North China which rendered their retention desirable. Further difficulties arose at the end of the year from the discovery that a projected road which we had regarded as the southern boundary of the site had been drawn on the plan so as to include two newly built houses within the area of the site. The difficulty of removing these houses has not yet been solved.

(d) Sino-British Cultural Association.

- 114. This association after a somewhat uncertain beginning is now in its third year and feeling its feet more strongly. Membership has increased to well over 200, and the new Elizabethan-style club house in Nanking will shortly be opened. The club will contain a large library and reading-room besides bedroom accommodation, and should give considerable impetus to the work of the association.
- 115. Among the more important activities of the association has been the establishment of professorships at leading Chinese universities. During 1936 four English professors have been engaged in lecturing on physics, English literature, hydraulic and mining engineering at the National Central, Wuhan, Chekiang and Peiyang Universities. Some difficulty has been encountered in securing two further professors of mechanical engineering and medicine for the Sun Yat-sen university in Canton and the National Health Administration in Nanking. The association's assistance has been requested by the National Agricultural Research Board, which has secured a grant of 20,000 dollars from the Board of Trustees of the British Boxer indemnity fund, in obtaining the services of two British experts in veterinary science and soils.
- 116. Professor Ifor Evans, head of the Department of English in the University of London, came to China in the autumn as the 1936 lecturer sent by the Universities China Committee. The corresponding Chinese lecturer to England was Dr. Chang Peng-chun. For 1937 the Universities China Committee has invited Dr. Li Chi, the noted archæologist, to visit England.
- 117. The association receives many enquiries from England about opportunities for service in Chinese universities. These enquiries are passed on to the leading universities and institutions of learning with details of the applicants and enquiries as to what openings are available. The lines along which services are mainly offered are anthropology, English, political science, sociology, French and German.

(e) Kuling Rendition Agreement.

118. This agreement was signed on the 30th December, 1935, by His Majesty's consul-general at Hankow, acting for the lot holders, and Mr. Chiang Chih-cheng, Director of the Bureau of Administration for Lushan. Its effect was to transfer the control of the Kuling Estate, hitherto a health resort for the exclusive use of foreigners, from the Kuling Estate Council, a foreign organisation under the protection of His Majesty's consulate-general at Hankow, to the Chinese. After protracted negotiation, the agreement was concluded in an atmosphere of marked cordiality, many tributes being paid to Mr. Moss from both foreign and Chinese quarters.

119. At present some confusion is being caused by the Chinese insistence on resurveying the whole estate, instead of simply issuing new Chinese title-deeds in place of the deeds issued by the council.

(f) Sasaki Case.

120. On the 26th May a Japanese officer named Sasaki, in the employ of the Manchukuo War Department, sustained serious injuries in a street brawl in Peking to which he subsequently succumbed. Reports were received at this Embassy that the Japanese authorities suspected that British soldiers belonging to the Embassy guard were implicated in the affair. On the 28th May Mr. Cowan, who was in charge of the Embassy at the time, called on Mr. Muto, the Secretary in charge of the Japanese Embassy, and requested that if the Japanese authorities really did suspect that the murder had been committed by a member of the British Embassy guard they should so inform the British Embassy with the least delay possible, so that enquiries might be effectively made. On the same day enquiries were begun spontaneously at this Embassy.

121. On the 30th May a note was received from the Japanese Embassy alleging that British soldiers were responsible for the crime. A military court of enquiry, which had to be sent up from Tientsin, was established on the 1st June, the earliest possible date. Meanwhile when Mr. Cowan asked the Japanese Embassy for leave to inspect the body, he was first told that this would be difficult to grant and afterwards it was admitted that the body had been cremated on the 29th May, the day before the Japanese note was handed in.

122. The court of enquiry held in the British Embassy on the 1st and 2nd June established that there were apparently no British troops either on pass or on duty outside the Embassy at the time of Sasaki's death. Moreover, the pack-supporting strap alleged by the Japanese authorities to have been found near the body was of a type quite different from those used by the British regiment stationed at Peking at the time.

123. The results of the preliminary investigation were communicated on the 2nd June by Mr. Cowan to the Japanese Embassy with an assurance that the most careful examination would be given to any further information which the Japanese Embassy might care to give. Documents containing evidence by various witnesses were subsequently submitted by the Japanese Embassy upon which they based accusations against British soldiers not only in connexion with the death of Sasaki, but also in connexion with an alleged assault in a Korean bar on a Japanese named Ohnishi.

124. The military court of enquiry reassembled on the 11th June, and an identification parade was held in the British Embassy barracks on the 12th June. (The reassembly of the court was delayed at the request of the Japanese Embassy, who desired to obtain authority from Tokyo for the Japanese witnesses to attend.) Three soldiers, Parrish, Cooke and Hunt, were identified by witnesses called by the Japanese Embassy as being involved in disturbances in bars on the night of the 26th May.

125. Proceedings of a preliminary examination were opened in the consular court at this Embassy on the 24th June. The prosecution, which was conducted by the Crown Advocate, at once stated that they did not wish to proceed against Parrish, who was thereupon discharged. Throughout the proceedings the work of the court was hampered by the failure of the Japanese authorities to produce

their witnesses at the time agreed upon. On the 3rd July the court found that there was insufficient evidence to frame any charge against either Cooke or Hunt in respect of the death of Sasaki, but that there was a *prima facie* case against Cooke in respect of an assault in a Korean bar on Ohnishi. The case against Cooke was then dealt with summarily and dismissed.

126. Following the termination of the above proceedings, a violent and almost hysterical campaign was launched in the local Peking and Tientsin Japanese press against the decisions of the court. Feeling amongst the Japanese community was further inflamed by statements issuing from the Japanese Embassy and, in particular, from General Matsumuro, the Japanese military spokesman, and serious incidents were feared. As a result of representations made to the Japanese Government by His Majesty's Ambassador in Tokyo, tension relaxed somewhat. Negotiations with regard to the matter were thereafter transferred to Tokyo, where it was eventually allowed to lapse. The three British soldiers involved in the incident were transferred to the home establishment later in the year.

127. On the night of the 25th August three British soldiers, returning to barracks in rickshaws, were fired upon by unknown assailants from a closed motor car. It was found impossible to establish the identity of the assailants or to produce evidence in support of the obvious inference that the attack was connected with the Sasaki case.

(3) Commonwealth of Australia.

128. In March a very daring flight was performed by Dr. Fenton, an Australian, from Port Darwin to Swatow in a "Gipsy Moth" machine. The object of Dr. Fenton's flight was to visit his mother who was in poor health following the death of his sister, who was the wife of the Netherlands consul at Swatow. Although Dr. Fenton reached Swatow without any papers, his machine was released by the Chinese authorities as a result of representations to the Waichiaopu by His Majesty's Ambassador and owing, no doubt, in part to the admiration of the Chinese officials for the example of filial piety displayed by Dr. Fenton.

129. The Chinese Government despatched a national flag and a goodwill message for the occasion of the centenary celebrations of South Australia.

(4) New Zealand.

130. Captain F. C. Chichester, accompanied by Mr. F. D. Herrick, reached Peking on the 12th August in a "Puss Moth" aeroplane, having flown there from New Zealand via Hong Kong, Foochow and Shanghai and Tsingtao. Mr. Chichester had intended to fly to England via Manchuria and the Union of Soviet Socialist Republics, but was forced to change his plans owing to the refusal of the Soviet authorities to grant permission for a flight across Russia. He accordingly left Peking on the 26th August with the intention of proceeding to England via Nanking, Hong Kong and India.

(5) Union of South Africa.

131. In January Mr. P. D. G. Gain, a director of Messrs. Slowe and Co. (Limited), a Shanghai British firm, was appointed Honorary Trade Commissioner in China for the Union of South Africa with headquarters at Shanghai. Mr. Gain is working in co-operation with Mr. A. T. Brennan, Union Trade Commissioner in the East, who is stationed at Batavia.

132. In September a despatch was received from His Majesty's Government in the Union of South Africa stating that Mr. Ping Yang-lei, Chinese consul at Johannesburg, had abused the Union liquor laws and requesting his recall. Following informal representations by His Majesty's Ambassador at Nanking, his Excellency was informed by the Chinese Political Vice-Minister for Foreign Affairs that Mr. Ping Yang-lei was being recalled to China for an enquiry. Mr. Chang Shou-mo (Assistant Director of the Department of International Affairs in the Chinese Ministry for Foreign Affairs) has since been appointed Chinese consul-general at Johannesburg.

(6) Burma.

133. As foreshadowed in last year's annual report (paragraph 102), the demarcation of the Burma-Yunnan frontier was not completed during the dry season 1935–36. This was in the main due to the procrastination and obstructive tactics in the field of the Chinese members of the Joint Commission and to the refusal of the chairman, Colonel Iselin, and the Chinese Government to support the British proposal to continue work beyond the beginning of April.

134. On instructions from His Majesty's Government, His Majesty's Chargé d'Affaires approached the Waichiaopu in the middle of July with the suggestion that, in order to avoid the expense and other difficulties entailed by another season in the field, an attempt should be made to reach an immediate settlement of the frontier dispute by direct negotiation in Nanking. The Chinese Government expressed their willingness to agree to this solution provided a suitable basis of agreement could be found. It was, however, found impossible to secure such a basis, and preparations for a second season in the field were accordingly proceeded with. Difficulties arose between His Majesty's Government and the Chinese Government with regard to the place and time of reassembly of the commission. It was finally decided to leave the place to the decision of the chairman, who chose Laochang, and His Majesty's Government agreed to the postponement of the date of reassembly until the 1st January, 1937 (they had suggested the 15th December, 1936), on the understanding that the work must be completed this season.

135. By an exchange of notes at Nanking, dated the 12th December, 1936, between His Majesty's Ambassador and the Chinese Minister for Foreign Affairs, it was agreed that article 11 of the "Convention between Great Britain and China relative to Burma and China of 1894," in so far as it relates to spirituous liquors, should be treated as null and void.

(7) Hong Kong.

136. Following the re-establishment of the Central Government's authority over the Province of Kwangtung, signs were rapidly forthcoming of the Central Government's desire to maintain and strengthen the good relations existing between Canton and Hong Kong. At the suggestion of the Chinese authorities, Sir Andrew Caldecott, the Governor of Hong Kong, and Lady Caldecott, paid a visit to Canton between the 17th and 19th September, where they were accorded an exceptionally warm welcome and met General and Mme. Chiang Kai-shek. On the 4th November this visit was returned by the chairman of the Kwangtung Provincial Government, General Huang Mu-sung, the Mayor of Canton, Mr. Tseng Yang-fu and Mr. Philip K. C. Tyau, special delegate for Foreign Affairs, accompanied by Mr. Phillips, His Majesty's consul-general at Canton. Both visits have resulted in an apparent increase in the friendly atmosphere surrounding the relations existing between the Government of Hong Kong and the Chinese Government.

again taking up with His Majesty's Ambassador in October the question of the evacuation of Chinese residents of Kowloon City, and requesting that the Hong Kong Government should be asked to cancel or suspend the decision for their removal. Simultaneous representations were made to His Majesty's consulgeneral at Canton by Dr. Philip K. C. Tyau, the special delegate for Foreign Affairs, in Canton, following a visit to Kowloon City undertaken by an emissary of his without the cognisance of the Hong Kong Government, an action which was resented by the Hong Kong Government. While discussions were still proceeding between His Majesty's Ambassador and the Hong Kong Government on this matter, a further memorandum was received from the Waichiaopu at the end of November again urging that in the interests of friendly relations between Great Britain and China, the decision of the Hong Kong Government should be cancelled or suspended. At the beginning of December the Governor of Hong Kong agreed, pending reference of the question to the Secretary of State for the Colonies, to suspend action for the removal of the Kowloon City residents, as he considered sanitary requirements to be met sufficiently for the time being by the immigration of those citizens who had accepted compensation.

- 138. In view of the fact that the proposed removal (with compensation) of the Kowloon residents to a healthier site could only be of benefit to them, it seems likely that the negative attitude of the Chinese Government in this matter is based on political considerations, viz., the non-admission by the Chinese Government of the validity of the Order in Council of 1899, under which Kowloon City was included in the administrative area of Hong Kong. This suspicion is confirmed by a conversation which took place between Mr. Hsu Mo, the Vice-Minister for Foreign Affairs, and a member of the staff of His Majesty's Embassy.
- 139. The Inspector-General of the Chinese Customs is in informal touch with the Hong Kong authorities, with a view to the reopening of the question of a customs agreement between China and Hong Kong on the lines of the abortive draft Hong Kong-China Trade and Customs Agreement of 1930 (see paragraph 357 of annual report for 1930). No official negotiations have yet been started.

(8) Straits Settlements and Malay States.

- 140. In June the Ministry of Interior's Gazette published instructions issued by that Ministry to the effect that applications for denationalisation from men below 45 years of age, if received after the 1st March, 1936, should not be forwarded to the Ministry but refused forthwith. The 1st March, 1936, was also the date designated by a mandate of the National Government of the 29th February, 1936, as the date of the enforcement of the Military Service Law (please see paragraph 321 of this report).
- 141. In reply to enquiries made by the military attaché as to whether a certificate of denationalisation would be refused to a British subject of Chinese race on the ground that he was under 45 years of age and therefore liable to military service, General Yang Hsuan-cheng, of the General Staff, stated that foreign Governments might claim those born of Chinese parents as their own citizens, but, nevertheless, the Chinese Government, in accordance with the relevant provisions of the Nationality Law, still claimed them as possessing Chinese nationality. The Ministry of the Interior, therefore, was obliged, in accordance with the relevant provisions of the Nationality Law and Military Service Law, not to accept petitions for denationalisation from any Chinese males under the age of 45 years, who would be under obligation to perform military service. In accordance with other provisions of this law, however, they would be exempted from service with the standing army, and would only be called upon for service with the citizen forces. Under certain conditions postponement of service would be granted.
- 142. The question of representations to the Chinese Government in regard to the effect of the above ruling on applications for denationalisation from British subjects of Chinese race born in Malaya was under consideration at the end of the year.

(B) Other Countries.

(1) Japan.

143. At the beginning of the year 1936 the position as between China and Japan was as follows: In order to prevent the break away of North China under pressure from the Kwantung Army the Central Government had authorised the establishment of a semi-autonomous régime to administer the provinces of Hopei and Chahar. The Kwantung Army, who were by no means satisfied with this solution of the North China question, had replied by creating a puppet State under their own protection out of the former demilitarised zone. General Chiang Kai-shek, who realised that there was no dealing with the Kwantung Army, left the Hopei-Chahar Political Affairs Council to fend for itself while he attempted to get a general settlement of Sino-Japanese problems with the Japanese Government through diplomatic channels, and in order to prepare a favourable atmosphere for diplomatic discussion he made a deliberate effort to reduce the tension in the relations between the two countries. The Japanese on their side contributed to the détente by refraining from provocatory military action, so that there was a refreshing freedom from the "incidents" which had been such a familiar feature of preceding months.

144. But almost at once fresh misunderstandings arose. In a speech before the Diet on the 21st January the Minister for Foreign Affairs, Mr. Hirota, re-enunciated his "three principles," the fundamentals of Japanese policy in China, namely: (1) the cessation of all anti-Japanese activities on the part of China and her active and effective collaboration with Japan; (2) the regularisation of relations between China and Manchukuo; and (3) the suppression of communism in China. Mr. Hirota went on to say that the Chinese Government had indicated its concurrence with the Japanese views and had suggested opening negotiations on this basis. This statement drew an immediate démenti from the Chinese Ministry for Foreign Affairs. The Central Government had in fact, not once but repeatedly, asserted that it would never sign any agreement detrimental to China's territorial and sovereign rights and there could be little doubt that the acceptance of Mr. Hirota's three principles as a basis for discussion would have had serious repercussions internally.

145. The chances of any general negotiations taking place, or proving fruitful if they did take place, seemed somewhat remote. The Japanese were indifferent to them, and seemed indeed quite content to allow the existing situation in North China to develop under the gentle guidance of the Kwantung Army; delay in its settlement was in the circumstances likely to be profitable to Japan rather than the reverse. Excuses for procrastination were ready to hand. First the Japanese Ambassador, Mr. Ariyoshi, was on the point of retirement, and it was announced that any general discussion of Sino-Japanese problems must await the arrival of his successor. The arrival of this successor, Mr. H. Arita, on the 26th February, coincided with the military coup in Tokyo, and he had hardly presented his credentials when he was recalled to Japan to become Minister for Foreign Affairs. Although he had a series of conversations with General Chang Chun between the 16th March and the 19th March it would seem that they did little more than emphasise the fundamental nature of the differences between the two countries.

Between the departure of Mr. Arita and the arrival of his successor, Mr. Kawagoe, there was an interval of three months, during which no negotiations took place in Nanking, but pressure was re-exerted on the northern officials for the expansion of so-called economic co-operation in North China. The smuggling, or as the Japanese termed it, the "special trade" through East Hopei also grew by leaps and bounds until at one time as much as two million dollars a week in revenue was being lost to the Central Government. It was so serious that it threatened the very stability of the country, but repeated official protests to the Japanese Government passed unheeded. While maintaining that smuggling was an internal affair for the suppression of which the Chinese alone were responsible, the Japanese made it impossible for them to suppress it by refusing (on the doubtful pretext that the Tangku Truce Agreement forbade the Chinese to keep armed forces in the demilitarised zone) to allow the Chinese to maintain armed preventive vessels in the territorial waters off the zone. It was indeed clear that the smuggling was being deliberately used by the Japanese as a means of bringing pressure to bear on the Chinese Government and compelling them to make concessions in the political and economic fields.

147. A further source of irritation was the increase in May of the Japanese garrison in North China to almost 7,000 men, a number considerably in excess of that required for its ostensible purpose of keeping open communication between Peking and the sea as provided by the Boxer Protocol of 1901. The Central Government formally protested against the increase, but again its protests were ignored. General Chiang Kai-shek informed His Majesty's Chargé d'Affaires on the 30th May that the situation at that time was very critical. He regarded the virtual military occupation of East Hopei, Peking, Tientsin and Fengtai as aggression which would justify a declaration of war; and though he was holding his hand on this occasion the limit had been reached, and if the Japanese went further and seized the Customs in North China or interfered with the existing system in any way he would treat such an act as a casus belli. This threat, when repeated to the Japanese Minister of War in Tokyo by the military attaché to His Majesty's Embassy, was treated with derision: the Japanese Government were quite convinced that General Chiang was not seriously contemplating a resort to war.

148. In the South-West, however, the increase of the Japanese garrison was seized upon as a rallying point for anti-Japanese sentiment, and there followed that strange crisis which has already been described in paragraphs 8 to 16 of this report. Mr. Kawogoe presented his credentials on the 3rd July while the crisis was at its height and entered on preliminary conversations with the Minister for Foreign Affairs, but it was not until September, after the settlement with the South-West, that formal negotiations were attempted. The anti-Japanese fever deliberately excited by the South-Western leaders brought as an aftermath a crop of incidents which further tangled the issues. On the 24th August a Chinese mob, enraged by the Japanese Government's determination to reopen their consulate at Chengtu in defiance of the Central Government's protests, attacked four Japanese visitors, killing two and severely injuring the others; on the 3rd September a Japanese subject was murdered at Pakhoi during an anti-Japanese demonstration fostered, so it was alleged, by the XIX Route Army of "Shanghai War" fame; on the 20th September a Japanese consular policeman was mysteriously shot dead in Hankow. While all these incidents roused Japanese feelings to passion heat, the increase in the strength of the Central Government arising from the settlement with the South-West gave the Chinese confidence and led to a stiffening of their attitude towards the Japanese demands.

149. In this atmosphere it was too much to hope that the diplomatic discussions would be fruitful. Contrary to expectations the Japanese Ambassador did not take up any of the recent incidents, but concentrated instead on a general settlement of Sino-Japanese relations: the incidents, he said, were of minor consequence and would settle themselves when the major problem was solved. The points which he was now putting forward were the following:-

(1) Sino-Japanese co-operation against the Communists, to extend all over China and not only to North China.

(2) The establishment of a special area in North China.

(3) Economic co-operation throughout China.

(4) The employment of Japanese advisers in all Government organs. (5) The reduction of tariffs on articles of special interest to the Japanese.

(6) The eradication of anti-Japanese feeling and suppression of anti-Japanese propaganda (including the revision of school text books). (7) The establishment of an air service between Fukuoka and Shanghai.

The Chinese replies to these points were as follows:—

(1) While they were doing all in their power to combat Communist activities they were not prepared to take any action which might seem to be aimed at a friendly Power. (Also they realised that the concession demanded by the Japanese would afford the latter an excuse for armed interference in any part of China.)

(2) They would not consider this in any circumstances.

(3) They were willing to explore all possibilities of genuine co-operation and, if necessary, to establish a joint Sino-Japanese organ for that purpose. (4) They were ready to engage a number of Japanese as technical advisers,

but not in the army and air force.

(5) They were ready to make some reductions but were not prepared to accept all Japanese desiderata irrespective of their effect on the Chinese revenue and the commerce of other Powers.

(6) They were doing all in their power to keep anti-Japanese feeling within limits, but the solution of this problem lay in the hands of the Japanese

themselves

(7) They were prepared to consider this when illegal Japanese flying in North China was brought to an end. The Chinese further maintained that any general settlement of Sino-Japanese relations must take into consideration Chinese grievances, and they cited particularly the abolition of the East Hopei Autonomous Government, the cancellation of the Tangku and Shanghai Armistice agreements and the suppression of smuggling in North China, of illegal flying, and of the activities of Korean ronin. Although it must always have been obvious that the Chinese had a case which must be considered, it appears that they formally presented it for the first time at an interview between General Chang Chun and Mr. Kawagoe on the 23rd September.

- 151. The Japanese Ambassador took immediate and violent exception to the interposition of these Chinese desiderata and broke off the interview. Within a few hours of this interview another murder was reported, this time of a Japanese seaman in Shanghai. The Chinese could not believe that now the Japanese Government would hold their hand, or that the Japanese army could be restrained from independent action. Envoys were hastily sent to Canton to report to General Chiang Kai-shek and take his instructions, while the reactions of the Japanese Government were anxiously awaited.
- 152. The Japanese Government were, however, no less embarrassed than the Chinese as to the proper course to pursue. While public opinion demanded some vigorous action to vindicate the murders of Japanese nationals in China, the Government were keenly aware that the Chinese were in a state of mind in which it would take little to drive them to desperate measures. They were equally aware of the watchful and hostile interest of the Soviet Government in their every move. They were accordingly determined to avoid, if possible, any action which might lead to hostilities and Mr. Kuwashima, head of the Asiatic Bureau in the Japanese Ministry for Foreign Affairs, was sent post-haste to Nanking with instructions to Mr. Kawagoe in this sense.
- 153. Mr. Kuwashima's arrival in Nanking on the 5th October coincided with the generalissimo's return. The latter received the Japanese Ambassador on the 8th October. The effect of the new instructions brought from Tokyo by Mr. Kuwashima was immediately apparent. According to the generalissimo's own version of this interview the Ambassador's attitude was most conciliatory; he pressed no demands, he admitted that there might be Chinese desiderata to be considered and he agreed that negotiations should proceed between himself and the Chinese Minister for Foreign Affairs. Having thus once more set matters in train, General Chiang only waited long enough to attend the celebration of the national day on the 10th October and again left Nanking. Though the pressure of his military and administrative duties gives him every excuse for these long absences, it is no secret that his main purpose is to keep the Japanese at arm's length and force them to deal with diplomatic questions through normal channels instead of going direct to him, as they would prefer.
- 154. Thereafter the diplomatic discussions were resumed between the Minister for Foreign Affairs and the Japanese Ambassador. The Japanese concentrated on their two main desiderata: co-operation against the Communists and the establishment of a special zone in North China. On these the Chinese were adamant and so the conversations dragged on fruitlessly until the middle of November, when they were interrupted by the Suiyuan incident mentioned in paragraphs 20 to 22 of this report. The news of the renewal of hostilities produced an immediate stiffening in the Chinese attitude; the Minister for Foreign Affairs refused to receive the Japanese Ambassador and let it be known that the conversations would not be renewed so long as the existing situation continued.
- 155. Another "incident" now occurred. Late in November strike fever spreading from Shanghai reached Tsingtao and affected a number of Japanese cotton mills, the situation being aggravated by political feeling roused by the invasion of Suiyuan. There was, however, no serious disturbance, and a settlement was in progress when the Japanese mill-owners on the 2nd December suddenly declared a lock-out in all mills. Japanese marines were landed who, in addition to policing the mills, searched municipal buildings and Kuomintang party offices, removed documents for examination and arrested nine persons. The reason given for these actions was that the strikes in the mills were fomented by agitators with the knowledge of the local authorities, who were not so active in the task of suppressing anti-Japanese movements as they should be, and various demands of a political nature were put forward. The trouble was localised and eventually settled without any serious concessions on the Chinese side.
- 156. As stated above (paragraph 154) the Minister for Foreign Affairs had refused to receive the Japanese Ambassador to continue the general political discussions. When the Tsingtao incident was reported, however, he sent for the Japanese Ambassador for the purpose of lodging a protest, and the Ambassador seized the opportunity to read to the Minister for Foreign Affairs a document purporting to be a résumé of the general negotiations up to date. The Minister for Foreign Affairs refused to accept it on the ground that it was inaccurate, since

it alleged that partial agreement had been reached in five out of the eight major "desiderata" of the Japanese (viz.: (1) direct China-Japan air service; (2) tariff revision; (3) control of Korean nationalists; (4) employment of Japanese advisers; and (5) restraint of anti-Japanese activities), while it took no account of the Chinese desiderata. Nevertheless, the Ambassador insisted on leaving the document, which was promptly sent after him by the Minister and as promptly returned by the Ambassador. Unwilling to continue this ignominious game the Chinese finally retained the document but informed the Japanese Embassy in writing that the contents were inaccurate, and at the same time issued a statement to the press dealing with the Japanese points seriatim as follows:—

(1) The question of a direct air service between Fukuoka and Shanghai had reached the stage of a draft agreement, but the Chinese Government refused to discuss the question further until illegal flying by Japanese planes in North China ceased.

(2) Tariffs could be adjusted to suit the requirements of trade and finance, but the first essential to a consideration of tariff adjustment was the suppression of smuggling and the restoration of the Customs' right of search.

(3) With regard to the activities of Korean nationalists the Chinese strongly discountenanced illegal activities of any sort by foreigners; but the Japanese must also curb the illegal activities of Koreans, Formosans and others committed under the ægis of Japan.

and others committed under the ægis of Japan.

(4) As regards advisers, the Chinese Government was in the habit of employing foreign advisers and would be prepared to employ Japanese as technical advisers if a favourable turn took place in Sino-Japanese relations.

(5) The Chinese Government was doing all in its power to produce harmonious relations and so prevent lawless actions on the part of its nationals, but a change of policy on Japan's part was the only real solution for anti-Japanese feeling.

157. Having failed to make any headway with their general settlement, the Japanese allowed these negotiations to go into cold storage and at last consented to discuss the individual incidents which they had hitherto refused to settle except as part of a general settlement. The Chinese had always been ready to give ample reparation for these acts of violence and in the last days of the year the Chengtu and Pakhoi incidents were settled by exchanges of notes in which it was recorded that the Chinese had punished the guilty and awarded compensation for the killed and injured.

Reference has already been made to the pressure exerted by the Japanese on the Northern officials for the expansion of so-called economic cooperation in North China. True co-operation has not made much progress. A company called the Hsing Chung Corporation has been brought into existence for the purpose of investing Japanese capital in economic and industrial development in North China and schemes are under consideration for the cultivation of cotton on a large scale, the construction of a railway from Shihchiachuang to Taku, the building of a port at Taku and the operation of iron mines at Lungyen; but none of these schemes has yet reached the practical stage. Japanese economic penetration has, however, made progress in other directions, as indicated by the purchase of a number of cotton mills in Tientsin and the controlling interest in the Yaohua Glass Company at Chinwangtao. On the 17th November this economic penetration was advanced one more stage by the inauguration of a Sino-Japanese air service between Manchukuo and the main towns in Chahar and North Hopei. The service is operated by a company formed for the purpose, i.e., the Huitung Corporation, the capital of which is, at least nominally, subscribed jointly by the Japanese and the Hopei-Chahar Council, but the aeroplanes and pilots are all Japanese. The action of General Sung Che-yuan (chairman of the Hopei-Chahar Council) in concluding such an agreement with out reference to the Central Government has been severely criticised in Chinese circles, but, if what General Sung said to His Majesty's Ambassador is to be believed, one of the secret provisions of the Ho-Umetsu Agreement was that certain air-lines should be established in Hopei and Chahar and he found it impossible to resist the pressure of the Japanese for the implementation of this provision. An implied term of the Huitung agreement was that upon the

inauguration of the new service all the illegal Japanese military air services in North China would cease. This understanding has not been implemented and Japanese military planes are still flying to Tientsin, Tsingtao and elsewhere.

(2) Union of Soviet Socialist Republics.

- 159. In the course of the year rumours, mostly from Japanese sources, continued to circulate alleging the existence of a Sino-Soviet Agreement.
- 160. At the end of June Mr. W. H. Donald, British adviser to General Chiang Kai-shek, drew the attention of His Majesty's Chargé d'Affaires to a document, alleged to be genuine, by the Japanese, purporting to contain the terms of Sino-Soviet "Military Alliance for Offensive and Defensive Purposes and Agreement of Mutual Aid." Mr. Donald stated that General Chiang Kai-shek denied the authenticity of this document.
- 161. From the information which has come into the hands of this Embassy during the past year there is nothing to prove the existence of any paper agreement between the Union of Soviet Socialist Republics and China, although it is possible and even probable that conversations and perhaps understandings have taken place. It is almost certain, for instance, that the Soviet representatives in China have for some time past been urging the Chinese to resist Japanese demands.
- 162. By the end of the year, however, it seemed unlikely that General Chiang Kai-shek had yet committed himself to a definite agreement with the Union of Soviet Socialist Republics.

(3) United States.

163. On the 28th May, 1936, an agreement was entered into between the Chinese Government and the Export and Import Bank of Washington, whereby the American Wheat and Flour Loan (1931) and the American Wheat and Cotton Loan (1933) were consolidated (see paragraph 63 of annual report for 1931 and paragraph 242 of annual report for 1933).

(4) France.

164. Early in the year the French Legation in China and the Chinese Legation at Paris were both elevated to the rank of Embassy. Mr. Wellington Koo presented his letters of credence to the President of the French Republic as first Chinese Ambassador to France on the 30th April, and M. Naggiar presented his to the President of the Chinese Republic as first French Ambassador to China on the 9th July, shortly after his arrival in China.

(5) Germany.

- . 165. At the end of May it was learnt on reliable authority that a barter agreement had been signed between the German Syndicate Hapro, represented in China by Herr Klein, and the Nanking authorities in respect of German arms and ammunition on one side and Chinese produce on the other. It appears that General von Reichenau, formerly Chef des Ministeramtes in Berlin, travelled to China specially to negotiate this agreement in collaboration with Herr Klein and that the German Embassy, as well as other German organisations in China, were kept completely in the dark about it.
- 166. It has consequently been difficult for this Embassy to obtain any reliable information about the agreement. It appears, however, that the Hapro Syndicate represents the German Government and that individual firms play no part in it. It has consequently caused much ill-feeling amongst independent German firms. Reports are conflicting as to the period over which the agreement is to extend, periods of one year, two years, five years and four periods of two years having been cited by various equally unreliable sources. All sources agree that the value of the goods covered by the agreement is 100 million dollars. It has not yet been found possible to verify the extent of the operations already concluded under the agreement.

167. Other information received tends to show that the agreement is not working as satisfactorily as had been hoped for owing (1) to the over-complicated nature of its structure; (2) to the antagonism created in China by the German-Japanese Agreement; and (3) to a feeling amongst the Chinese that the Germans intend to profit from the agreement at their expense.

(6) Siam.

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168. Sino-Siamese relations appear to have benefited from the visit to Siam from the 6th June to the 4th July of a Chinese goodwill mission headed by Dr. Ling Ping, a representative of the Ministry of Education.

(7) League of Nations.

169. On the 1st October the League Assembly decided to create two temporary seats on the League Council, each for three years. One of these seats will be occupied by China.

(8) Italo-Ethiopian War.

170. In May the Chinese Government received a communication from the Italian Government, similar to one received by His Majesty's Government announcing the annexation of the Ethiopian Empire by Italy and the assumption by the King of Italy of the title of Emperor of Ethiopia. The Chinese Government followed the example of His Majesty's Government and returned no reply to this communication.

(9) International Settlement, Shanghai.

(a) Council Elections.

171. When in 1935 the question was discussed as to the attitude which should be adopted by the British in face of the Japanese challenge to the predominant position of the former in the administration of the International Settlement, the view was taken that every effort should be made to maintain the existing number of British seats on the council, meeting the Japanese pressure by concessions in regard to increased Japanese personnel in the administration, by effecting economies in the administration and in other directions. When, accordingly, it was learnt that the Japanese proposed to try to secure increased representation on the council at the expense of a British candidate at the municipal elections, the British vote was mobilised by an Election Committee appointed for the purpose by representative British organisations, with the result that the three Japanese candidates found themselves at the bottom of the poll and all five British candidates were elected. It was afterwards discovered that a serious error had been made in the count in circumstances which reflected unfavourably on the efficiency of British members of the Council secretariat. The result of the election was, however, not affected by the miscount, and though the Japanese at first demanded a new election they eventually decided to withdraw one of their candidates, thus rendering a fresh poll unnecessary.

(b) Chinese Representation on the Council.

The Chinese demand for increased representation on the council was renewed during the year. The demand is founded on the contention that representation should be based either on the numerical strengths of the various nationalities or on the proportion of taxes paid. The foreign contention is that in order to maintain the foreign control of the settlement it is essential that the foreign element on the council should not be in danger of being out-voted by the Chinese element. In August the Mayor of the Shanghai City Government transmitted to the senior consul with his support a proposal from the Chinese Ratepayers' Association that the number of Chinese counsellors be increased from five to nine, thus making an equal number of Chinese and non-Chinese on the council. The senior consul replied by reminding the mayor that the council instituted under the Land Regulations was composed only of foreign members; it had, he added, in course of time been thought desirable that Chinese representatives should be admitted to voice the sentiments and wishes of the Chinese community, and the consular body were of opinion that this community were already well represented, with five councillors, eleven committeemen and two land commissioners, and that there was no danger of the Chinese side of any question remaining unheard for lack of spokesmen.

(c) Secretary-General's Post.

173. Mr. Stirling Fessenden, the present secretary-general, is likely to retire before long on account of age and the question of his successor has been agitating the minds of the council. Mr. Jones, the next senior official in the secretariat, was not regarded as temperamentally suitable for the post, and occasion was taken of the ballot episode (see paragraph 171) to secure his retirement. Mr. G. G. Phillips, hitherto deputy secretary, has accordingly become secretary, with the reversion of Mr. Fessenden's post, for which he is deemed to have the necessary qualifications and disposition.

(d) Financial Situation of Council.

174. Shanghai, like the rest of the world, has been suffering from a slump in business. Though the municipal taxes are exceedingly low, judged by foreign standards, attempts to increase them even in good times lead to agitation and disorder, since the Chinese are led to believe that they are being mulcted for the benefit of the privileged foreigners and an extravagant administration. At the present time the prospect is one which the council are reluctant to face, the more so that Japanese ratepayers would, in all likelihood, join the opposition on this occasion in order to further their own ends, and every effort has accordingly been made to effect economies in the administration.

175. Among economies already effected are: an all-round reduction in the salaries of council employees, the abolition of the Press Information Bureau and the Rickshaw Board, and the disbandment of some of the less useful units of the Volunteer Corps. A tentative suggestion by the secretary-general that the whole corps might in certain circumstances be disbanded was strongly opposed by the British naval and military authorities.

(e) Japanese Demand for Increased Personnel in Police Force.

176. In November the Japanese consul-general presented the chairman of the Shanghai Municipal Council with demands that the British assistant commissioner in charge of Hongkew Division and the British inspectors in charge of three police stations in the eastern and northern districts should be replaced by Japanese, and that there should be a general increase in the number of Japanese police employed in this area. The matter was discussed by His Majesty's Ambassador with His Majesty's consul-general, the chairman of the council and council officials, and the view was taken that it would be advisable to continue the discussions with the Japanese consul-general in a liberal spirit, in order to see if some fairly innocuous compromise could be reached.

(f) Factory Legislation: Application in International Settlement.

177. Negotiations conducted by the secretary-general of the Shanghai Municipal Council and the City Government on the thorny subject of factory inspection in the settlement resulted in June in a draft agreement whereby the municipal council, "under authority delegated by the Chinese authorities," undertook to apply within the settlement those portions of the Chinese factory laws which were enforced in Chinese territory; an inspectorate to be established within the council for this purpose and to consist of inspectors nominated in equal numbers by the Chinese authorities and the council. When the draft agreement was considered by the consular body, the Japanese consul-general objected to it as constituting a serious violation of the fundamental principles of the extraterritorial status and administrative integrity of the settlement and of the extraterritorial rights of the Powers concerned, and he refused to accept it unless it was amended so as to make it clear that the Chinese law could only be applied to factories not protected by extra-territorial status. This lead was followed in varying degrees by the representatives of the other extra-territorial countries, and the draft agreement was referred back to the council with the request that an attempt be made to amend it in the desired sense.

(g) Land Regulations Amendment.

178. The foreign view of the Land Regulations is that they are the basic law or constitution of the International Settlement and give validity to the foreign municipal administration. The Chinese officials, who naturally resent all

encroachments on the sovereignty of their country, adopt the attitude that the Land Regulations have never been formally ratified by the Central Government and therefore are invalid *ab initio*. As far as possible they refuse to give them any formal recognition. In the case of amendments to the Land Regulations, where such have been clearly in the interest of the Chinese, as when Chinese councillors were admitted to the council in 1926, the authorities have agreed to and confirmed the changes in principle but have never been brought to agree to the necessary amendment of the wording of the Land Regulations to cover these changes.

179. During the past year the council, being anxious to incorporate the changes in the printed official copies of the regulations, raised the question whether, in the circumstances, the explicit approval of the Chinese Government was necessary. The consular body, to whom the enquiry was addressed, took the line that it would be unwise to seek the explicit approval of the Chinese authorities, since it was certain to be refused, but that the amendments should be embodied in the printed regulations and a copy then sent to the Chinese authorities for their information with an explanation that the changes merely covered matters to which they had already agreed.

(h) Ward Road Gaol.

180. Conditions in the gaol have continued to be the subject of correspondence as the result of criticisms levelled at them by Miss Marjory Fry. So far as this question came up during the year 1936, it dealt particularly with the condition of young persons sentenced to reformatory treatment and to the high mortality rate. The reply of the municipal council was that the fault lay not with them but with the Chinese court, which in the first case destroyed the effect of reformatory treatment by a sentence of imprisonment to follow the treatment, and in the second case inflicted sentences of imprisonment without regard to the health of the prisoners, a high proportion of whom are opium and narcotic addicts. The gaol was visited on the 29th June by His Majesty's Chargé d'Affaires, who was favourably impressed by the conditions he saw there.

(10) Treaties.

Tabular Statement.

With—Between—.	Place and Date of Signature.	Subject,	Place and Date of Exchange or Deposit of Ratifications.	Date of Entry into Force.	Remarks.
With His Majesty's Govern- ment in the United Kingdom	Nanking, December 12, 1986	Exchange of notes regarding the rendering null and void of Article XI of the Convention between Great Britain and China. Relative to Burma and China 1894 in so far as it relates to spirituous liquors.			
Between Kiangsi Provincial Government and Council of the Kuling Estate	Kuling, December 30, 1935	Exchange of notes regarding rendition of Kuling Estate to the Kiangsi Provincial Government.			
With Latvia	London, June 25, 1936	Treaty of Amity	***		Notified by Chinese Govern on November 21, 1936. I fications not exchanged by of year.
Between Chinese Govern- ment and Export and Import Bank of Washing- ton	Washington, May 28, 1936	Exchange of notes regarding consolidation of American Wheat and Flour Loan (1931) and American Wheat and Cotton Loan (1933).			
With Japan	Nanking, December 30, 1936	Exchange of notes regarding settlement of Chengtu and Pakhoi incidents (murder of Japanese citizens).			

III.—RAILWAYS.

182. The year has been remarkable for activity in connexion with the construction of new railways and the settlement of indebtedness under the old railway loans. No progress has been made on the lines of General Hammond's suggestions for a comprehensive settlement and for the reorganisation of the Railway Administration (see paragraph 157 of annual report 1935). With regard to the latter, the question of the establishment of a central board of control with foreign advisers, and that of the appointment of foreign experts to controlling posts on the individual railways, are under consideration. In this connexion informal representations are to be made with a view to the appointment by the Ministry of Railways of a British expert to supervise specifications issued for railway materials bought in the United Kingdom through the Boxer Indemnity Purchasing Commission.

The Peking-Mukden Railway (Peking-Shanhaikuan section) has for all practical purposes been abstracted, for the time being at least, from the control of the Ministry of Railways at Nanking (see paragraph 145 of annual report 1935), and has since early in 1936 been nominally controlled by the Communications Commission of the Hopei-Chahar Political Council. The position of the (British) general manager and engineer-in-chief has become that of a mere figurehead, and effective control is in the hands of the pro-Japanese managing director appointed at the beginning of the year. A through traffic agreement with the South Manchuria Railway came into force on the 1st May, 1936. The Chinese engineer, who had long been on friendly terms both with the British and Chinese Corporation and with the Kailan Mining Administration, resigned his post in November. In November the control of Peitaiho Beach (a portion of the coast in the vicinity of which contraband has been principally run ashore) was handed over to the East Hopei Autonomous Government; there is reason to believe that arrangements are under consideration for handing over to the same authorities the policing of the line from Shanhaikuan to Tongku, for handing over to the South Manchuria Railway the control of the whole line from Mukden to Peking, and for the redemption of the outstanding portion of the 1898 loan. The terms of a loan agreement contracted in May 1935 (without the knowledge of the Embassy and constituting incidentally an infringement both of the 1898 loan and of the Fengehing loan) between the Kailan Mining Administration and the Ministry of Railways (for further particulars, see the mining section of this report) have on the instructions of the Hopei-Chahar Political Council and contrary to the instructions of the Ministry been repudiated by the Peking-Mukden Railway Administration. It is understood that the Administration now contributes 300,000 dollars a month to the Hopei-Chahar Political Council and 100,000 dollars a month to the East Hopei Autonomous Government, and makes no contribution to the Ministry; monthly sums of £5,000, however, continue to be paid in respect of the indebtedness under the Fengching loan and the service of the 1898 loan continues to be regularly met.

184. The monthly instalments of £5,000 have been regularly continued from the revenues of the Peking–Mukden Railway for the liquidation of indebtedness under the Chinese Government 6 per Cent. Shanghai–Fengching Railway Mortgage Redemption Loan of 1914 (see paragraph 146 of annual report 1935). Sums of £9,022 10s., £7,894 13s. 9d., and £7,894 13s. 9d. (in payment of instalments of interest and bank's commission) and a sum of £37,593 15s. (in payment of an instalment of amortisation, plus bank's commission), were remitted to London from the special reserve account in February, October, December and August. The balance at credit in this account at the end of December was £7,542 12s. 3d.; according to the schedule which has been drawn up the next payment will be made in July or August 1937 of an instalment of amortisation of £37,500, plus bank's commission.

185. The service of the Shanghai–Nanking Railway Loan, 1903, is now in arrears as to three half-yearly instalments of interest and seven annual instalments of principal, the total arrears amounting to £1,023,352 (see paragraph 148 of annual report 1935). On final payment in March 1936 of the Rolling-Stock Loan of 1929 the percentage of gross earnings paid every ten days into the special reserve account was reduced from 10 per cent. to $7\frac{1}{2}$ per cent.; of the monthly sum in this account, two-thirds are set aside to repay the overdraft

of 2 million dollars with the Shanghai Commercial and Savings Bank (arranged by the Ministry of Railways through the Bank of China) which had enabled the railway to pay in November 1935 the half-yearly instalment of interest due in June 1934; the remaining one-third is set aside to meet the British and Chinese Corporation's one-fifth share of the net profits for the year 1933 and the half-year ending the 30th June, 1934. With regard to the latter the amount due to the corporation is subject to the decision of the arbitrators in a dispute as to the allocation of losses and damages incurred by the railway during the Sino-Japanese troubles of 1932. In addition to this ten-daily payment into the special reserve account, the railway has since the 25th May, 1936, set aside weekly in a Special Loan Service Account with the Hong Kong and Shanghai Banking Corporation in London a sum of £2,500 as provision for the service of the original 1903 loan.

186. No payments have yet been made in respect of the advances (or interest thereon) made by the British and Chinese Corporation under the Pukow–Sinyang Railway Loan Agreement of 1913 (see paragraph 150 of annual report 1935). The construction of an extension (which is reported to be under consideration) of the Huainan Railway from Yochiachi to Sinyang to connect with a branch from Hofei would constitute virtual unilateral abrogation of the agreement and would entitle the British and Chinese Corporation to claim repayment of the advances as well as payment of the interest thereon.

187. No payments have yet been made in respect of the advances (or interest thereon) made by the British and Chinese Corporation under the Nanking-Hunan Railway Loan Agreement of 1914 (see paragraph 149 of annual report 1935). The Ministry of Railways has now concluded an agreement with the Hong Kong and Shanghai Banking Corporation and the Jardine Engineering Corporation (into which, however, the British and Chinese Corporation do not enter) for the supply of materials for the construction of the Hsuancheng (Ningkuofu)–Kweichi section of the Nanking–Kiangsi Railway. As this constitutes the final step in the unilateral abrogation of the Nanking–Hunan Railway Loan Agreement representations have now again been made urging repayment of the advances themselves as well as payment of the interest thereon.

188. The settlement of indebtedness under the Lunghai Railway Loan, on terms very unfavourable to the Belgian investors, has been followed by a new loan of £3 million from Dutch and Belgian interests to finance the south-westward extension of the line from Paoki (on the Shensi-Kansu border) to Chengtu (see paragraph 162 of annual report 1935). Survey is in progress on the Paoki-Tienshui section of the projected westward extension to Lanchow (Kansu).

189. On the 24th September, 1936, the Waichiaopu transmitted to this Embassy an offer in the following terms, announced on the 25th February, 1936, by the Ministries of Finance and Railways, concerning the resumption of the service of bonds of the Tientsin-Pukow Railway Loans of 1908 and 1910 (see paragraph 151 of annual report 1935): Interest at 2½ per cent. per annum in 1936, 1937 and 1938 and 5 per cent. thereafter, paid from railway revenue (guaranteed by customs revenue); four-fifths of interest in arrears and of short-paid interest in 1936–38 to be cancelled, and non-interest-bearing scrip to be issued for the remaining one-fifth and paid by instalments, beginning in 1941, over a period of approximately twenty years; the principal to be paid out of railway revenue beginning in 1940, the amount of annual payments to be dependent upon the gross earnings, so that the loan should be liquidated within about forty years from 1936. In connexion with this offer, the Minister of Railways accepted proposals for the appointment of a Loan Service Committee, and the appointment of foreign officials on the railway. This offer was accepted in February 1936 by the representative in Shanghai of the Bondholders' Committee in London. Regulations governing the organisation of the Loan Service Committee were adopted by the Executive Yuan in April 1936 and simultaneously put into force. Final acceptance of the offer, however, appears to have been delayed owing to the reluctance of the British bondholders to agree to the terms on which the Minister of Railways proposed to settle the claims of the Deutsch-Asiatische Bank in respect of the advances made to the Ministry of Communications against the 1910 issue for the purpose of completing the construction of the line. It seems clear that a settlement of this point will involve

some modification of the offer made in February 1936. The negotiations for a settlement, in which the financial adviser has taken an active part, have been conducted in China by a representative of the Hong Kong and Shanghai Bank on behalf of the bondholders. No request has been made by the Chinese Central Railways for representations by this Embassy.

190. An offer was made by the Minister of Railways on the 17th March, 1936, for the settlement of the indebtedness under the Hukuang Railways Loan (see paragraph 152 of annual report 1935) on the following terms: Interest to be paid at the rate of $2\frac{1}{2}$ per cent. per annum in 1936–39 inclusive, and thereafter at 5 per cent. per annum; interest in arrears to be calculated at 1 per cent. per annum simple interest; non-interest-bearing scrip to be issued for arrears of interest and also for one-fifth of the difference between the $2\frac{1}{2}$ per cent. interest to be paid during 1936–39 and the 5 per cent. interest which is to be paid after 1939—this scrip being paid as from 1942 over approximately a period of twenty years. This offer has not yet been accepted owing, it is understood, to efforts of the American group to secure better terms, and to the fact that negotiations regarding the appointment of foreign railway officials and of a board of commissioners to supervise the administration have not been concluded. The Financial Adviser has taken an active part in the negotiations for this settlement, but the intervention of the Embassy has not been called for.

191. The Canton–Kowloon Railway Sterling Advance of 1925 (see paragraph 153 of annual report 1935) was finally paid off on the 4th May, 1936. An offer for the settlement of indebtedness under the 1907 loan was made by the Ministry of Railways on the 26th August, and is understood to have been accepted by the bondholders (see paragraph 156 of annual report 1935). The question of the loop line to connect with the Canton–Hankow Railway has been much discussed, and there seems reason to suppose it may shortly be constructed.

192. The first through train on the Canton–Hankow Railway left Canton on the 1st September, 1936, and reached Wuchang on the 3rd.

The Shanghai-Hangchow-Ningpo Railway Completion Loan of 1934 (see paragraph 147 of annual report 1935) was superseded on the 8th May, 1936, by the Chinese Government 6 per cent. Sterling Shanghai-Hangchow-Ningpo Railway Completion Loan of the Twenty-Fifth Year of the Republic of China, signed between the Ministries of Railways and Finance on the one part, and a syndicate consisting of the British and Chinese Corporation and of the China Development Finance Corporation on the other part. The agreement provides for repayment of the advances made by the syndicate in 1935, for the completion of the railway, including the construction of the Chien Tang River bridge (see paragraph 290 of annual report 1935), for the construction of branches to connect the bridge with the railway and with the Chekiang-Kiangsi Railway, and for the liquidation of certain outstanding debts of the railway. Funds were also secretly provided with which the Chinese were able to construct the strategic Soochow-Kashing loop-line apparently from their own resources, so avoiding the protest which the Japanese would have made to a loan for the purpose. agreement calls for the establishment of a Loan Service Committee, on which the Ministry of Railways and the syndicate are represented. If materials are purchased abroad out of the loan funds preference is to be given to parties recommended by the syndicate, and the latter has agreed that this proviso shall be exercised in favour of British manufacturers. In spite of the fact that only a small portion of the proceeds were to be expended in the United Kingdom, the Chancellor of the Exchequer as a special measure consented to a quotation of the loan on the London Stock Exchange. The 1935 advances by the syndicate were duly repaid on the 15th June.

194. On the 23rd April, 1936, the Peking Syndicate (Limited), concluded agreements with the Ministry of Railways in settlement of the obligations outstanding under the Taokow-Chinghua Railway Loan Agreement. (The Chinese Government Honan Railway 5 per Cent. Gold Loan, 1905, the Ching Meng Loan Agreement of 1920, and the Hundred Wagon Loan Agreement of 1919.) The Tao-Ching Railway is now administered as a branch of the Peking-Hangkow Railway (see paragraph 161 of annual report 1935). Payments due under the new agreements are being regularly made. With financial assistance from the Peking Syndicate, it has been extended north-eastwards as far as Chuwang on

the Wei River near the Honan-Hopei border, and will shortly be opened to traffic Regulations for the organisation of the Tsinan-Liaocheng Railway (a westward extension of the Kiaotsi Railway) were promulgated by the Executive Yuan in June, and the earth-work has been completed, but actual construction appears to be in abeyance, possibly owing to Japanese insistence on participating in the project (see paragraph 161 of annual report 1935).

- 195. The Yushan–Nanchang section of the Chekiang–Kiangsi Railway was formally opened on the 15th January (see paragraph 167 of annual report 1935). On the 1st February, 1936, the Ministry of Railways issued the Railway Reconstruction Loan Second Issue for the construction of the westward extension of this line from Nanchang to Pinghsiang: a loan agreement was signed on the 11th February between the Chekiang–Kiangsi United Railway Corporation and the Bank of China (acting on its own behalf and also as trustees for a group of Chinese banks and also for Otto Wolff), and a contract was signed between the bank and Otto Wolff by which the latter is to supply on credit the construction materials required.
- 196. An agreement is reported to have been signed at Shanghai on the 16th December, 1936, between the newly inaugurated Szechuan–Kweichow Railway Corporation (represented by the China Development Finance Corporation) and a French syndicate represented by the Banque Franco-Chinoise pour le Commerce et l'Industrie, for the construction of the Chungking–Chengtu Railway (see paragraph 159 of annual report 1935). It is understood that the first instalment (40 million dollars issued on the 1st March, 1936) of the Railway Reconstruction Loan Third Issue (120 million dollars), authorised on the 25th February, 1936, is to be employed for the financing of this line.
- On the 4th December, 1936, the Ministry of Railways signed two agreements to provide for the construction of the (Sunchiapu) Hsuancheng-Kweichi section of the Nanking-Kiangsi Railway (see paragraph 165 of annual report 1935). The first, between the Ministry and the Board of Trustees for the Administration of the British Boxer Indemnity funds, provides for a loan of £450,000 secured on the surplus of the railway revenues (including surtax) already pledged to the Board for the existing loan to the Canton-Hankow Railway (see paragraph 148 of annual report 1934), over and above the sum required for the service of that loan, on the similar estimated surplus anticipated earnings of the new railway, and on the amortised capital of the Canton-Hankow Railway Loan. The same security forms the basis of the complementary agreement, between the Ministry of Railways and the Hong Kong and Shanghai Banking Corporation and the Jardine Engineering Corporation, for the provision of a further sum of £450,000. The total amount of £900,000 is to be applied for the purchase of materials in the United Kingdom. The same security also forms the basis of a cash loan from Chinese banks of 14 million dollars to finance the construction of the line. The manner in which the Boxer funds have thus been "stretched" to cover further purchases in the United Kingdom is explained in another section of this report. An interesting feature of these agreements is that the sterling loans have been given priority over the local currency loan both as regards repayment of principal and payment of interest.
- 198. The Yunnanfu-Talifu-Tengyueh-Burma Railway project, for which Messrs. Pauling and Co. obtained the concession in 1913, has again been under discussion but is not apparently being seriously pursued.
- 199. The commercial counsellor was informed on the 20th September by the Minister of Railways that he had been instructed by the generalissimo (because of Japanese pressure for economic control throughout China, and in order to forestall Japanese objections) to conclude within the next six months, preferably with British interests, agreements to build: a railway from Lungchang on the Chungking-Chengtu Railway southwards to Kweiyang and thence through Liuchow in Kwangsi to Canton; and also a railway from Canton northwards to a point west of Swatow and thence ultimately to connect with the Kiangnan Railway at a point in Chekiang. In November the Minister of Railways supplied the commercial counsellor with an up-to-date map and memorandum from which it appears that the Kwangtung section of the Canton to Chekiang line, and the

Lungchang–Kweiyang and Liuchow–Samshui sections of the Lungchang to Canton line, are projects to which the Ministry wishes to give priority. On this occasion the Minister of Railways stated that, though for political reasons he would like to come to preliminary agreements with British interests, he did not think the Government should proceed with their construction in the immediate fuure. It appears, however, that if possible, the Canton–Meihsien section of the Canton–Swatow project will be undertaken forthwith.

- 200. A project in which the Japanese have been actively concerned is the construction of a line from Shihchiachwang (a station on the Peking–Hankow Railway and the terminus of the Chengtai Railway) through Tsangchow (a station on the Tientsin–Pukow Railway) to Tientsin. The negotiations have been principally conducted between the pro-Japanese managing-director of the Peking–Mukden Railway and the Japanese President of the Hsing Chung Kung Ssu. It appears that the construction of this line has been approved by the Hopei–Chahar Political Council, that the final agreements will in effect provide for the supply of technical experts and materials by the South Manchuria Railway, but that the actual route and the details of the financing of the project have not yet been decided. Economically and strategically the line is of great importance.
- 201. Other railway projects in which the Japanese are believed to have shown interest are the westward extensions of the Shantung Railway and the Peking-Suiyuan Railway, the completion of the Tung-Pu Railway (see paragraph 163 of annual report 1935), and the construction of a projected line through Fukien from north to south.
- 202. For fear of Japanese opposition the Chinese found it necessary to make secret provision (under the terms of the Shanghai–Hangchow–Ningpo Completion Loan) for the construction of the Soochow–Kashing loop-line.
- 203. The Japanese attitude towards railway construction in China has been a factor of importance in the consideration of such questions by this Embassy. It appears that they insist on a pretension which the Chinese (at least so far as concerns China north of the Yellow River) are not at the moment prepared to contest, to participate in the financing of, and the supply of materials for, all new railways.
- 204. The Kawasaki Company (controlled by the Japanese navy) have requested Messrs. J. Stone and Co. to extend their licence for manufacturing and selling train lighting sets to cover not only Japan and Manchuria, but also railways in North China.
- 205. Japanese co-operation appears to be a primary condition for the security of any long-term market loan for railway construction, and the possibility of revising consortium arrangements (with the inclusion of the Chinese) has been under consideration and discussion.

IV.—SHIPPING.

- 206. In May the reply of the Hong Kong Government was received to the Chinese Government's note of November 1935 regarding the non-acceptance by the Hong Kong Government of Chinese passenger certificates issued in connexion with the Safety of Life at Sea Convention as being of equal validity with those issued by the Hong Kong Government (please see paragraph 169 of annual report for 1935). The Hong Kong Government stated that they could not admit that China's accession to the convention necessarily implied acceptance by other authorities of China's passenger certificates and that they could not at present recognise these certificates because the Chinese regulations were not sufficiently detailed to enable their value to be estimated. The Hong Kong Government's attitude was duly communicated to the Chinese Government, but by the end of the year no further communication on this subject had been received from them.
- 207. In July, at the request of the Government of Hong Kong, His Majesty's Chargé d'Affaires drew the attention of the Chinese Government to the case of the discrepancies discovered by the marine surveyor at Hong Kong between the condition of the Chinese steamship *Ha Yih* and her safety certificate issued by the Chinese Government (see paragraph 170 of annual report for 1935). The

attention of the Chinese Government was drawn to the friction and delay which are bound to occur in the clearance of Chinese passenger ships at Hong Kong unless care is taken by the appropriate department of the Chinese Government to ensure that the particulars on the Safety Certificate correspond exactly with the actual conditions on board the ship and with the requirements of the Safety of Life at Sea Convention.

208. In April, on instructions from the Foreign Office, His Majesty's Embassy communicated to the Chinese Government, who had acceded to the International Load Line Convention of 1930 on the 19th August, 1935, the legal position in the United Kingdom with respect to the supervision of ships in United Kingdom ports in the matter of overloading, with the request that His Majesty's Government might be informed of what control was being exercised in China in the matter.

209. The Chinese Government replied that they were still engaged in preparations for applying effective control and would address a further communication as soon as the requisite measures had been drawn up. In the meantime the method employed previous to China's accession would be retained, i.e., a tidewaiter would always be despatched by the Maritime Customs to superintend the observance of the Load Line limit when ships were being loaded.

 $210.\,$ The affairs of the China Merchants' Steam Navigation Company have continued in a highly unsatisfactory condition. Following the resignation $en\ bloc$ of the previous board of directors and board of supervisors in February, a new general manager and assistant general manager were appointed on the 10th February, and the administration of the company was reconstituted in accordance with regulations promulgated by the Ministry of Communications on the 8th February, the general effect of which was to place control of the company in the hands of the Ministry of Communications (see paragraph 177 of annual report 1935). The financial condition of the company remains deplorable; the Export Credits Guarantee Department have refused assistance in connexion with the purchase of new steamers, and, in connexion with a revised list of the company's requirements, the commercial counsellor and the financial adviser have advised that, before consideration can be given to purchases by the company on terms of deferred payment, its finances and management must be thoroughly reorganised. It has been ascertained that the company is unable to meet payments due by it to the board of trustees for the British Boxer indemnity funds. Instalments of payment of the pensions and other retiring allowances due to British ex-employees of the company (see paragraph 178 of annual report 1935) have eventually been met, but on every occasion in arrears and only after representations have been made. Negotiations, in which the financial adviser has participated, for a settlement of the Hong Kong and Shanghai Bank's claim against the company have not yet been satisfactorily concluded. A proposal that Messrs. Jardine, Matheson and Co. (Limited) and Messrs. Butterfield and Swire might on terms take over the management of the company was under serious consideration in the early part of the year, but has been in abeyance since May. No progress has been made with the secret preliminary discussions between Messrs. Butterfield and Swire and the Ministry of Communications for some form of co-operation between the British company and the Chinese company

211. A reply was received from the Waichiaopu on the 25th January, 1936, categorically repudiating and rebutting all the arguments advanced by this Embassy to induce the issue by the Ministry of Railways to British shipping companies of through rail and water bills of lading, such as are issued to the China Merchants' Steam Navigation Company. The British shipping companies have now come to realise that for the time being at least they are suffering from very little actual discrimination, since it has transpired that the China Merchants' through bill of lading facilities have not proved popular. Messrs. Jardine, Matheson and Co. and Messrs. Butterfield and Swire are, meanwhile, understood to be working out independent schemes by which they may themselves be enabled to issue what will in effect be through bills of lading.

212. With regard to the port of Laoyao (Lienyunkang), Messrs. Butterfield and Swire were able on the 31st May to berth one of their ships without difficulty, to discharge a small quantity of oil and sugar and to collect a cargo of general

produce; it seemed, therefore, that the right of British vessels to trade in the port under inland water pass had been established in principle. In October, however, the firm were informed by the Customs that they would not be permitted to clear one of their vessels for the port; as the result of representations which had been made to the authorities concerned at Nanking to the effect that, if Chinese merchant vessels were allowed to use the port, British merchant ships should also be allowed to do so, it is understood that the Chinese Government proposed to close the port to all merchant shipping in order to prevent its use by the Japanese.

- 213. The general question of the Pilotage Regulations has remained dormant throughout the year. The question of replacement of vacancies at Shanghai, however, became pressing early in the year, and an arrangement was come to in June between the Shanghai Licensed Pilots' Association and the Customs, with the consular body, except the Japanese consul-general, consenting. This arrangement, which was put forward by the Chinese authorities, provided for the filling of the three vacancies by the appointment of two British pilots and one German without prejudice to the right of the Chinese Government to appoint Chinese pilots irrespective of quota, and in effect upheld the principle of the pilotage fee quota and temporarily limited the total number of Chinese pilots to six; moreover, a Chinese was to be appointed only when a vacancy occurred among the pilots of a country whose representation was in excess of the quota. The Japanese consul-general notified His Majesty's consul-general and senior consul at Shanghai that his Government objected to the arrangement as a departure from the 1868 Pilotage Regulations, and reserved the right to abandon the quota system and negotiate separately with the Chinese Government for an increase in the number of Chinese pilots.
- 214. Certain difficulties occurred in connexion with the vessels owned by Messrs. G. L. Shaw and Co. at Antung. An attempt was made by the Japanese authorities to station Japanese police on board their ships trading between Chefoo, Tsingtao, Dairen and Antung, but was withdrawn as a result of representations made in Tokyo by His Majesty's Ambassador, and locally by His Majesty's consul-general at Mukden. Subsequently, Mr. Shaw complained of discrimination against his vessels in the matter of the coolie trade between the above-mentioned ports. A Japanese company, called the Tatung Kung-ssu, with headquarters at Hsinking, had been established in March 1935, the functions of which were to control movement of Chinese coolies to Manchuria, entrance being restricted to those holding its certificates, and Mr. Shaw alleged that by the refusal of the Tatung Kung-ssu to issue certificates to coolies travelling by his ships to Dairen and Antung discrimination was being practised against his ships in favour of a new shipping combine formed at Dairen on the 1st June, 1936, which his firm had not been allowed to join. The question is now under investigation with a view to establishing proofs of the alleged discrimination.
- 215. The search of Messrs. Jardine, Matheson and Co.'s hulk at Wuhu on the 30th July by members of the local Opium Suppression Supervisory Bureau formed the subject of representations to the Waichiaopu, as a result of which an undertaking was given by the latter that further searches would not be carried out except in accordance with "established procedure," i.e., by the Maritime Customs.
- 216. The Ichang Salt Assistant Auditorate came to an arrangement with the Maritime Customs, effective from the 7th September, whereby all merchant vessels entering Ichang are searched by a salt examining party under the control of the Customs. The arrangement referred to in paragraph 189 of the 1935 annual report was not carried out as the Hupei Salt Auditorate were unwilling to obtain the stamp of His Majesty's consul at Ichang.
- 217. The steamship A poey, a British ship registered at Hong Kong, was on the 19th October searched while in port at Shanghai by detectives and armed police alleged to be connected with the Salt Revenue Department of the Chinese Government, and a Chinese member of the crew arrested. His Majesty's consul-general protested to the Chief Inspectors of Salt Revenue against the flagrant disregard of the rights of a vessel under the British flag. A reply was received expressing regrets at the prescribed procedure not having been followed, and stating that instructions had been issued to those concerned with a view to effective measures being taken to avoid a repetition of such incidents.

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- 218. On the 14th September the steamship Tailee, a British ship registered in Hong Kong, was fired on from the shore near Kongmoon, one Chinese quarter-master being killed and the master (British) and one lady passenger (American) slightly wounded. Strong representations were made by His Majesty's consulgeneral at Canton to the local authorities and a vice-consul was sent to the spot to investigate. Proclamations were issued by the Chinese authorities to villages along the river bank forbidding such firing in future, and orders were given for the arrest of the culprits. Since, however, it transpired that the Tailee had for years had a bad reputation for excessive speed, contrary to warnings, which it was alleged had destroyed dykes and flooded riparian land, and so led to the firing in question, His Majesty's consul-general proposed not to press the case strongly, and this attitude received the approval of His Majesty's Embassy.
- The carriage of Chinese troops by British steamers plying on the West River has formed the subjest of correspondence with his Excellency the Commander-in-chief, China Station, and His Majesty's consul-general at Canton. As a result of a case which occurred in June 1936, it became obvious that cases of British ships carrying armed Chinese troops contrary to standing instructions had been of fairly frequent occurrence, and his Excellency the Commander-inchief accordingly recommended that: (1) small parties of armed Chinese troops might be carried provided their arms were given up; (2) if information was received that armed troops were being carried without the arms being given up and without report by the shipping company concerned, British protection might be withdrawn, and in the case of irresponsible firms British registration might be cancelled; and (3) written orders to be issued by the high Chinese authorities to the military officers concerned along the West River laying down the maximum number to travel in one vessel and that they must surrender their arms, masters of vessels to be furnished with a signed copy of this order, and some form of certificate to acompany each party of troops for identification purposes. Recommendation No. 1 was carried out by a circular letter addressed by His Majesty's consul-general at Canton to the shipping companies concerned on the 15th July, but owing to unstaple political conditions it has not yet been possible to introduce the detailed procedure suggested under No. 3; action in regard to No. 2 was still under consideration at the close of the year, but it is to be noted that, while under the China Ports Amendment Regulations, 1928 (King's Regulations No. 1 of 1928) the inherent power lies in His Majesty's Secretary of State to direct that British protection shall not be accorded to a British-registered vessel, it is not possible under existing legislation for the registry of a British ship or the registration of a British company to be cancelled.

V.—MINING.

- 220. Neither the affairs of the Sino-British Mentoukou Coal Mining Company nor those of the Pekin Syndicate have given rise to any anxiety in 1936. A settlement of indebtedness under the Pekin Syndicate's loan to the Honan Provincial Government of 1925 is understood to have reached by an exchange of letters dated the 15th July, 1936, between the syndicate and the Honan Provincial Government.
- 221. On the 18th May, 1936, Declarations of Trust and Joint Interest giving effect to clause 17 of the Supplemental Agreement of 1934 (see paragraph 176 of annual report 1934) were signed between the Lanchow Mining Company and the Chinese Engineering and Mining Company (Limited).
- 222. There have been no signs that the Japanese military or other authorities have actually brought pressure to bear to force the British interests in the Kailan Mining Administration out of business. The Belgian interests in the Yaohwa Glass Factory at Chinwangtao, of which the Kailan Mining Administration act as general managers, have been sold out to Japanese. In November information was received to the effect that the Nippon Sangyo Company had stated that they would like to buy up the company or companies which constitute the Kailan Mining Administration, but there have been no developments in this connexion. The Kailan Mining Administration have appointed two Japanese to be members of their staff as go-betweens in any dealings which may be necessary with the Japanese authorities, but they have not been appointed as a result of pressure by the latter. As a result of intrigues by certain shareholders in the

Lanchow Mining Company abortive attempts have been made to oust the Chinese co-chief manager of the administration; on the first occasion the new appointee presented himself at the administration's offices with a formal appointment from the chairman of the Hopei-Chahar Political Council, on the second occasion the same candidate proposed to arrange matters by an intrigue with the Mayor of Tientsin, provided that he was assured there would be no opposition from this Embassy.

223. The relations of the administration with the Peiping-Liaoning Railway have given rise to some anxiety. Early in February the railway attempted to bring pressure to bear on the administration to alter the terms of existing agreements for the carriage of the administration's products and for the supply of coal and coke, and veiled threats were used that the railway might obtain assistance from the Japanese. In November the administration informed the Embassy that the railway, acting on the instructions of the Hopei-Chahar Political Council, had stated in writing that they were not prepared to carry out the terms of an agreement which had been concluded in May 1935 between the administration and the Ministry of Railways, under which (a) the administration had advanced to the Ministry a sum of 2 million dollars, which was to be repaid by deductions from freight owing by the administration to the railway; and (b) the administration retained ownership and control of certain rolling-stock on the railway. The existence of this loan agreement of 1935, which contravenes the provisions of the Shanghai–Fengching Railway Mortgage Redemption Loan and the provisions of the original Peking–Mukden Railway Loan, had not previously been disclosed by the administration to this Embassy. Representations have been made to the chairman of the council to the effect that the railway should be instructed to comply with the terms of the Loan Agreement, and to the Waichiaopu, with a reservation of the right to make further representations in so far as the Fengching and Peking-Mukden Railway agreements are concerned.

224. On the 27th February the East Hopei Autonomous Government issued a mandate providing for payment of the Mining Products Tax to its own tax collection office, for supplemental registration of mining rights in the autonomous area with the East Hopei Bureau of Reconstruction, and for payment of the Mining Area Tax on such property to this bureau. Stocks of coal covered by tax certificates which were issued previously by the (National) Consolidated Tax Bureau and which had up to then enabled coal to be shipped were approaching exhaustion, and the East Hopei Autonomous Government continued to press the Administration to pay to them, instead of to the (National) Consolidated Tax Bureau, the Mining Products Tax against which only fresh certificates could be issued. By paying in advance to the Ministry of Industries in 1933 1 million dollars (covering half of ten years' Mining Area Tax), and by a further payment of 134,000 dollars to the Ministry for the lease of a disputed portion of the mine field in 1935, the Administration obtained in 1935 a mining permit, without registration either of the Chinese Engineering and Mining Company or of the Kailan Mining Administration as a Chinese Company, as required by Chinese law, and, moreover, contrary to the Chinese Mining Law the permit was endorsed as good for renewal on expiry. It was clear that compliance with the demand made for supplemental registration with the Autonomous Government and for payment of the Mining Area Tax to that Government might lead to difficulties, more especially as no portion of the Mining Area Tax payable by the Administration is free until the 1st July, 1938; one half being retained by the Administration for repayment of the advance made in 1933, and the remaining half being used for repayment of a loan obtained in 1934 from Chinese banks by the Ministry of Industries. The possibility of making representations either to the Japanese Government in Tokyo, or to the local Japanese authorities in North China, was carefully considered, but no action was eventually deemed advisable. Administration in April obtained a further supply of certificates from the Consolidated Tax Bureau on payment of the appropriate amount of the Mining Products Tax, and no difficulty was experienced in this connexion from the East Hopei authorities. On the 26th June the Administration wrote to the East Hopei Autonomous Government explaining that owing to the fact that the Administration was a joint Sino-British enterprise, the question of supplemental registration was a complicated one and it might be difficult to comply within the time-limit imposed, and the Administration continued to play for time in connexion with this question of supplemental registration of their mining permit. The Administration informed the Embassy in October that: the mines area had been resurveyed in accordance with the requirements of the Ministry of Industries; that the plan had been sealed and endorsed by the Ministry of Industries and sealed by the Hopei Bureau of Reconstruction; that the Administration's mining permit had been officially registered by the Hopei Bureau of Reconstruction; and that the mining permit formerly issued to the Lanchow Mining Company had been duly cancelled. In the Statement of Matters for Registration which has now been issued by the Hopei Commissioner for Reconstruction, it is explicitly stated that an extension of the mining permit may be granted.

VI.—TAXATION.

- 225. "Illegal" taxation continues to be levied in Fukien, Shensi, Kwangtung, and Szechuan (see paragraph 263 of annual report, 1935). On the 26th February the foreign oil companies at Canton signed a new agreement for further advance payment of kerosene tax of 5 million dollars (see paragraph 196 of annual report, 1934), but on the 27th July the Canton Custom-House reimposed the national rates of import duty on "liquid fuels": in September, however, an agreement was reached by which the Kerosene Business Tax is continued at the reduced rate of 1 dollar per unit, a portion only being paid in cash while the balance is credited against the advance.
- 226. A dispute between the Hopei-Chahar Political Council and the Ministry of Finance as to the allocation of the Consolidated Tax on Rolled Tobacco, in the course of which the Tientsin market was denuded of British American Tobacco Company's cigarettes and which threatened to disrupt the consolidated tax system throughout North China, was eventually settled by the resumption of the payment by the Ministry of Finance through the company to the council of the monthly subsidy of 500,000 dollars. In the area controlled by the East Hopei Autonomous Government, however, the company continues to pay the taxation locally demanded and to deduct the amount from the sums paid to the Internal Revenue Administration at Shanghai.
- On the 28th August, 1936, His Majesty's Chargé d'Affaires received a communication from the Waichiaopu enclosing a printed copy of the Provisional Ordinance Governing Income Tax and requesting that all British subjects residing in China be instructed to comply therewith. A similar communication was addressed to the other interested heads of mission. The ordinance had been promulgated by the National Government on the 21st July, and a further mandate on the 2nd September provided that the ordinance should come into force on the 1st October, but that the tax should be levied as from that date only on the emoluments and salaries of public functionaries and on interest derived from Government bonds and deposits; and that it should be levied on other items as from the 1st January, 1937. The American Ambassador replied that the regulations could not be considered applicable to American citizens, and the French Ambassador reserved French rights and requested the issue of instructions so that no misunderstandings might arise. His Majesty's Chargé d'Affaires merely informed the Waichiaopu that translations of their note and enclosures had been forwarded to the Foreign Office. If the Chinese authorities press the matter they will be informed informally that unless and until the tax is generally paid by Chinese and other foreign nationals throughout China there can be no question of making the law applicable to British subjects. Detailed enforcement regulations were promulgated on the 22nd August, 1936, and put into force on the 1st October, on which date also the levy of the tax on the salaries of Government employees and on the interest on Government bonds and bank deposits was put into effect. Further notes were addressed by the Waichiaopu to some interested heads of mission (but not to this Embassy) on the 30th December requesting that foreign nationals be instructed to comply with the regulations.
- 228. Deductions in respect of income-tax are, in effect, being made on the salaries of Government employees, both Chinese and foreign, and also on the interest on Government bonds, which is deducted at source. It appears that the Hopei-Chahar Political Council has proposed that the levy of the tax in the area under its administration should be postponed. A proposal that the income-tax should be collected from exterritorial foreigners by the customs, or by a separate

foreign-controlled organisation similar to the Customs Administration, has been under consideration, as has also a proposal that British banks should assist in the collection of the tax by deducting it from the salaries of their employees and from interest on bank deposits.

- 229. There has been a general extension in the collection of business tax of from Chinese throughout the country, and the Szechuan Provincial Government in June 1936 requested His Majesty's consul to assist in its collection from British subjects. The question, however, was not pressed and has not been raised elsewhere.
- 230. Repeated representations have been made to the Waichiaopu with regard to the discriminary provisions of the Stamp Tax Law in regard to bills of lading. Modifications in the tax schedule which were introduced in January 1936 went some way towards obviating in practice some of the objections which had been made to the law by the British Chamber of Commerce. It is understood that a further revision is in contemplation which would remove the discriminatory provisions in regard to bills of lading (see paragraph 265 of annual report 1935).
- 231. An ordinance (differing little from the provisional regulations published in 1935) governing the imposition of the Consolidated Tax on Alcohol was promulgated by the National Government on the 8th October, 1936, and came into force the same day (see paragraph 267 of annual report 1935).
- In reply to a request from the British Chamber of Commerce at Shanghai that His Majesty's Government would define their attitude towards the proviso as regards discrimination which was contained in the offer of the 27th January, 1927, to the effect that "His Majesty's Government are prepared to make British subjects in China liable to pay such regular and legal Chinese taxation not involving discrimination against British subjects or British goods as is in fact imposed on and paid by Chinese citizens throughout China, British Chamber of Commerce at Shanghai, and the committees of other British Chambers of Commerce in China, have been confidentially informed that would, in the view of His Majesty's Government, be unfair discrimination against British subjects to make them legally liable to pay a tax which the nationals of other Powers did not pay:" they have, however, at the same time been reminded that, "though it is the policy of His Majesty's Government to give the fullest possible support to British merchants in resisting encroachment on treaty rights which might jeopardise their position in China, it is not possible for His Majesty's Government to guarantee that resistance to taxation which is not recognised as applicable to British subjects can in every case be successfully maintained, nor can it be laid down as an axiom that resistance rather than compromise is in every case the wisest course to pursue. It will be difficult, therefore, for British merchants, so long as present conditions in China continue, to escape the necessity of estimating for themselves the risks involved in adopting or in maintaining too long what may prove to have been too rigid an attitude. If a tax is legal, reasonable in amount and generally paid by Chinese, British subjects would be well advised, in their own interests, to pay it, whatever attitude the nationals of other Powers may adopt"; and they have at the same time been informed that, "in the event of a proposal to make British subjects legally liable to pay a Chinese tax becoming the subject of actual negotiations, His Majesty's Government would take into consideration all the circumstances of the case, including both the intrinsic difficulties of applying Chinese tax regulations to British subjectsespecially in the case of a direct tax such as the business tax or income-tax-and the extent of the failure or inability of the Chinese Government to secure observance of the tax regulations by the nationals of other Powers: if it were considered to be desirable to continue the negotiations to a conclusion, His Majesty's Government would aim at reaching some workable arrangement that would be in the best interests of the British merchants concerned."

VII.—TRADE.

233. Regulations providing for a complete monopoly of the manufacture and sale of mixed chemical fertilisers, which were enforced by the Provincial Governments of Chekiang and Kiangsu, have formed the subject of official protests by His Majesty's consular officers concerned and by this Embassy (see paragraph 299 of annual report 1934).

234. On the 22nd June His Majesty's Chargé d'Affaires interviewed the Minister of Industries on the subject of a proposal by the Chinese Government to establish a China vegetable Oil Corporation, designed apparently to exercise certain monopolistic functions in connexion with the wood-oil trade. At this interview the Minister of Industries assured His Majesty's Chargé d'Affaires that the Chinese Government had no intention of interfering in any way with the present freedom of the foreign owners of existing installations to carry on the business in their own way, but he made the proviso that the permission of the Chinese Government must be obtained before new installations could be erected or existing installations extended. It appeared, nevertheless, that the corporation were determined if possible to circumvent this assurance, and His Majesty's Chargé d'Affaires therefore once again addressed the Minister of Industries asking whether British owners of installations could still count on the observance in the spirit as well as in the letter of the assurances which had been given. No reply was received to this letter, and reports received from Chungking indicated that the corporation were, in fact, about to take action which would involve direct interference with British traders in wood oil; early in November His Majesty's Ambassador therefore wrote to the Minister of Industries requesting his assurance that any such activities on the part of the corporation were contrary to his wishes and that instructions would be issued to the corporation accordingly. subsequent interview the Minister of Industries insisted that the Chinese Government wanted freedom of trade and were not trying to establish a monopoly of the wood oil business. Eventually His Majesty's Ambassador received an oral message from the Minister of Industries to the effect that he had instructed the Reconstruction Commissioner for Szechuan to settle the matter. Similar general representions regarding the monopolistic tendencies of the corporation were made by the American Ambassador.

235. On the 27th July, 1936, His Majesty's consul-general at Canton addressed a note to the Provincial Government of Kwangsi protesting against the operation of the Kwangsi Import and Export Trading Bureau on the grounds that its establishment was contrary to the monopoly provisions of the treaties and that its activities were inflicting serious injury to British merchants. A reply was received from the Provincial Government dated the 15th September, 1936, declining to accept the contention that this monopoly was inflicting damage on British trade and indicating no intention of considering its abolition. His Majesty's consul-general was instructed to address a further communication to the Provincial Government stating that he could not accept their reply as final and reserving our rights under the treaties.

236. The situation with regard to the grant of rewards under the Law for the Encouragement of Industrial Technique and the Law for the Encouragement of Industrial Enterprises (see paragraph 296 of annual report 1935), remains unchanged. In reply to the representations made in 1935 regarding monopoly rights of manufacture granted to two Chinese cigarette paper factories, the Waichiaopu on the 14th January, 1936, sent in a memorandum denying that there was any conflict with treaty rights, and stating that the treaty provisions which had been cited related to freedom of trade and commerce and not to rights of manufacture in industry. On the 24th March the Minister for Foreign Affairs was formally informed that His Majesty's Government are not prepared to concur in an interpretation of the treaty provisions in question which limits their application in the manner suggested.

237. It appears that steps have been taken to put into force some at least of the measures agreed upon in 1935 to deal with the problem of hand-rolled cigarettes (see paragraph 305 of annual report 1935). In connexion with these measures, however, the Ministry of Finance has had under consideration schemes for the control of the production and sale of tobacco leaf which seemed to involve, or to pave the way for, a Government monopoly; representations have, therefore, accordingly been made both by this Embassy and by the American Embassy against the institution of any system of control which would result in such a monopoly. The British-American Tobacco Company are, however, now considering, in conjunction with the Ministry of Finance, one such scheme.

238. In April 1936 His Majesty's consul-general at Hankow received a communication from the Special Foreign Affairs Deputy stating that the Public

Sales Bureaux and the monopolies in salt and oil conducted by the co-operative societies in Kiangsi were to be abolished; at the same time the Kiukiang agent of the Asiatic Petroleum Company stated that free trade in oil had been re-established in the province (see paragraph 304 of annual report 1935.)

- 239. On the 1st January, 1936, an "Antimony Control Bureau" under the control of the Central Government at Nanking took the place of the former Hunan Antimony Syndicate. On the 8th January, 1936, the chairman of the Hunan Provincial Government informed His Majesty's consul at Changsha that there was no intention of creating a monopoly and that antimony merchants would in fact have far more freedom under the new régime than under the old (see paragraph 300 of annual report 1935).
- 240. In May 1936 a China Black Tea Trading Bureau (under the Chinese Black Tea Trading Commission of Anhwei and Kiangsi), was established at Shanghai. An agreement was finally reached with the foreign tea exporters which, while not entirely satisfactory, permits of trade being done through the accustomed channels (though in a modified form), and eliminates the more pronounced monopolistic features of the scheme as originally conceived.
- 241. The Ministry of Finance and the Ministry of Industries have granted a petition of the Chinese Match Manufacturers' Association for the establishment of an "organisation for the administration of all affairs relative to joint production and sales of matches manufactured in China." This union has concluded agreements with the Japanese match factories in North China under which the latter become members, and it is understood that the American Far Eastern Match Company have also come to a working agreement with the union. The attitude of the American Embassy is that the establishment of the union is tantamount to monopoly control of the match industry in China, and that they are unable, consequently, to associate themselves in any way with the steps taken by the American company to join the union, although in fact there appear to be no American stock-holders in the company, and should it remain outside the union the American Embassy is unlikely to take strong action in their defence (see paragraph 285 of annual report 1935).
- 242. In his first public utterance in Canton in August 1936 Marshal Chiang Kai-shek is reported to have severely denounced the provincial monopolies which had been "introduced by corrupt officials to swell their own coffers." Nevertheless, from information subsequently received, it appears that it is the intention of the Government to continue at least the monopolies on fertilisers, cement and sugar. The present liabilities of the Kwangtung provincial factories are believed to amount to no less than 14 million dollars (see paragraphs 297, 298 and 299 of annual report 1935).
- 243. Owing to the system of permits which is in force it is in practice impossible for foreign importers of cement to compete with the Government factories.
- 244. Information was received in February from which it appeared that the Government sugar mills were again occupied with crushing cane and producing white sugar therefrom, and that they were no longer processing imported sugars.
- 245. After a final unsatisfactory decision by the Administrative Court in the "Hazeline Snow" case, and in view of the fact that the China Soap Company were contemplating an appeal to the Executive Yuan in the "Lux" case (see paragraph 311 of annual report 1935), His Majesty's Chargé d'Affaires in July wrote to the Minister of Industries drawing attention to the fact that under article 14 of the Trade-Mark Law (now article 13 of the revised law) as applied by the courts, the exclusive right to the use of a mark is confined to the goods specified in the application for registration and that between the articles in different groups there is no restriction, and suggesting means by which this defect of the law as administered might be remedied. At the same time the Trade-Mark Sub-Committee of the British Chamber of Commerce entered upon a campaign of publicity to be followed up by diplomatic representations. A memorandum was drawn up by the Chamber emphasising the lack of protection under the existing law as at present administered of registered marks against the use of similar marks on goods in other categories, that is to say, urging

reduction of the categories so as to widen the scope of each, the right of protest against the registration of any mark, and/or discretionary powers to the examiners in the Trade-Mark Bureau to reject any mark; the memorandum also drew attention to the provisions of the Trade-Mark Law to which reference had been made in the memorials of 1935 and which had not been modified in the new Chinese Trade-Mark Law as revised and promulgated in November 1935. At the same time the Sino-British Trade Council at Shanghai drew up a memorandum on similar lines which was signed by the Chinese President of the Council and sent to the Minister of Industries. On the 13th November His Majesty's Ambassador wrote to the Minister of Industries recalling the representations which had been made in 1935 and 1936 summarising the views of the British Chamber of Commerce, and requesting that the defects in the law might be remedied. On the 27th November the Minister of Industries replied that he would instruct the Trade-Mark Bureau to give its attention to the points mentioned at the next revision of the law.

- 246. In view of the reshuffle which had taken place in the personnel of the Ministry of Industries, the attention of the Minister of Industries was drawn in February to the representations which had been made in 1935 on the subject of the Insurance Enterprise Law (see paragraph 385 of annual report 1935). It being ascertained that the Insurance Enterprise Law was in process of revision, a memorandum was addressed to the Waichiaopu on the 16th December, 1936, calling attention to the representations previously made and expressing the hope that due weight had been given to them in the course of revision of the law. It appears that the law as eventually adopted by the Legislative Yuan on the 27th November (but not yet enforced) does not meet any of the objections which were made to the draft law, and the question of further representations is being considered. At the same time the Legislative Yuan also approved a law relating to the application of the Insurance Enterprise Law (enforcement regulations), and an Insurance Law dealing with the contract between the insurer and the insured.
- 247. Agreements for the construction of the Kwangtung Iron and Steel Works were signed in Canton on the 28th April on behalf of the Kwangtung Provincial Government and Messrs. H. A. Brassert and Co. (Limited) (see paragraph 289 of annual report 1935). It is understood that in November 1936 Marshal Chiang Kai-shek approved the project subject to the following conditions: that the steel works in Hunan, the contract for which now seems certain to go to a German firm, should be proceeded with; that the control and general direction of both projects should be in the hands of the Nanking Government; and that a programme should be drawn up as regards rolling, price and other matters, to ensure that the two works should not compete, or conflict in matters of policy (see paragraph 289 of annual report 1935).
- 248. It was announced in December that the Executive Yuan had enacted regulations for the formation of a special "Committee to Supervise the Nation's Steel and Iron Works."
- 249. Sino-British Trade Councils were formed in Shanghai and at Hankow early in 1936. It has proved impossible to establish any organisation analogous to a "Grievances Committee," which was originally contemplated in connexion with the loan proposals in 1935, to serve as a report centre in which various Sino-British Trade Councils as they were formed might usefully communicate their observations on important matters affecting Sino-British trade as a whole.
- 250. On the 4th December, 1936, the National Government issued an order explaining a ruling given in 1934 to the effect that no loan agreement concluded by the Central Government or any local authorities would be valid unless authorised by the National Government; whereas reference was previously made to loan agreements only, it is now specifically laid down that all discussions between provincial and municipal Governments and foreigners, and all agreements made by these Governments providing for the investment of capital jointly with foreigners, do not acquire validity without the approval of the Central Government.
- 251. A secret Sino-German Barter Agreement is understood to have been concluded in April 1936. It seems clear that German merchants, and German

officials resident in China, have no extensive or definite information regarding this agreement. It appears that the agreement provides for barter arrangements as between the German and Chinese Governments in which individual firms play no part, that the goods to be supplied by Germany consist in the main of munitions, and that China in return is to supply principally wolfram and other light metals. All informants are agreed that the amount of goods covered by the agreement is 100 million dollars, but reports as to the period over which the agreement is to extend are conflicting. There is considerable divergence of opinion as to the extent of the operations which have already been concluded under the agreement, but it would appear to be substantial. The effect on the operation of this agreement of the recent agreement between Germany and Japan is not yet fully obvious, but it is clear that it has been adverse.

252. The question of the disabilities under which creditors suffer when endeavouring to realise on property pledged as security for credit facilities (see paragraph 282 of annual report 1935), and also the question of the action of the Chinese authorities in rent cases, have again been under consideration, but no satisfactory solution of either problem has yet been reached.

253. Negotiations, in which the financial adviser has given his assistance, have continued for a settlement of the debt of the China Merchants Steam Navigation Company to the Hong Kong and Shanghai Banking Corporation (see paragraphs 177 and 282 of annual report 1935). The bank has found itself unable to accept the best terms which the Ministry of Finance is prepared to offer and a deadlock has been reached.

VIII.—CUSTOMS AND TARIFFS.

254. The questions of the resumption of the recruitment of foreigners for the Customs Service, of the increase of the Japanese personnel, and of the nationality of the next inspector-general have formed the subject of discussions throughout the year with the Chinese and Japanese authorities (see paragraphs 326 and 327 of annual report 1935). While the Chinese have displayed no willingness to resume the recruitment of foreigners or to meet the Japanese in any way (except by the appointment of additional Japanese staff at Tsingtao, where conditions are peculiar), it appears as the result of discussions at Tokyo in September between His Majesty's Ambassador to China and the Japanese Minister for Foreign Affairs that we and the Japanese are in entire agreement as to the following desiderata, though a favourable opportunity must be awaited before any action can usefully be taken:—

Mr. Kishimoto should be immediately appointed deputy inspector-general, and a suitable British subject appointed to succeed him as chief secretary; immediate resumption of recruitment of British and other foreigners in such a way as gradually and rapidly to increase the number of Japanese until they are numerically equal to the British personnel; an assurance that suitable British and Japanese successors will be selected for Sir Frederick Maze and Mr. Kishimoto, the posts of deputy inspector-general and chief secretary being always held respectively by Japanese and British subjects; the ultimate succession to the post of inspector-general to be left open for future discussion and decision.

255. Smuggling (see paragraphs 331–336 of annual report 1935) has, with unimportant exceptions, been confined to imports into the East Hopei Autonomous area, where, under the terms of the Tangku Truce, the Japanese still refuse to permit the effective rearming of the Customs Preventive Service. It is estimated that import duties evaded amount to over 50 million dollars, but the bulk of these goods would not have been imported except as contraband, and the decrease in the Tientsin custom-house revenues for 1936, as compared with 1935, was only ½ million dollars, all of which cannot be attributed to smuggling. Smuggling into Tientsin and the East Hopei Autonomous Area continues unabated, but the Chinese authorities have enforced measures to prevent the distribution of contraband from Tientsin, which have proved effective except so far as Peking, Central Southern Hopei, and a small area in North-Western Shantung are concerned. The liquidation of stocks of contraband in Tientsin is one of the problems which will demand solution before any settlement of this question can be reached.

- 256. British importers of oil and sugar from Dutch sources have suffered heavy losses, but the direct effect on United Kingdom trade has been negligible. The indirect effect in disorganisation of established channels of trade, in unsettling the market, and in undermining national credit, is imponderable, but is probably less serious than was anticipated.
- 257. The whole question has been the subject of repeated representations in London, Tokyo and Nanking, by the Foreign Office, by His Majesty's Ambassadors in China and Japan, and by Sir Frederick Leith-Ross, to the principal Chinese and Japanese authorities concerned. It has been made amply clear that His Majesty's Government regards the restoration to the Customs of effective control in this area as a matter of the first importance.
- 258. As a result of the extension of Central Government authority, smuggling conditions in Fukien and Kwangtung have greatly improved.
- 259. Measures enforced by the Chinese authorities to prevent the transportation inland and distribution of contraband have been acquiesced in, except by the Japanese, and have given rise to no serious interference with British trade.
- 260. On the 17th March a memorandum was addressed by the Ministry for Foreign Affairs to the Embassy explaining that the Customs Preventive Ordinance and revised Manifest Regulations (see paragraph 338 of annual report, 1935) in no way conflict with the Sino-British treaties. In reply, a note was addressed to the Minister for Foreign Affairs stating that His Majesty's Government do not concur and reserve their rights under the treaties.
- 261. In April a Customs notification was issued to the effect that merchants protesting against penalties imposed by the commissioners must do so to the Customs Penalty Board and not to the ordinary law courts.
- 262. With regard to the application in China of section 259 of the Customs Consolidation Act of 1876 (see paragraph 337 of annual report, 1935), the judge of His Majesty's Supreme Court has expressed the opinion, in which the Crown Advocate concurs, that this section cannot be applied in China, under the provisions of article 39 (2) of the China Order in Council, 1925, to the prosecutions of British subjects for offences under article 74. The question of redrafting article 74 is still under consideration.
- 263. There have been no cases of unreasonable penalties inflicted on British subjects or British ships in smuggling cases during the year.
- 264. The possibility of reopening negotiations for the conclusion of a customs agreement is under informal consideration by the Hong Kong and the Customs authorities; in this connexion the question of a regional preferential tariff has been mooted by certain sections of the Hong Kong mercantile community.
- 265. In connexion with Sino-Japanese relations in general the question of a modification of the import tariff has been under serious consideration, but when those negotiations were broken off this question also fell into abeyance. The Minister of Finance informed the commercial counsellor in November that the Chinese Government would not entertain any preferential proposal.
- 266. The collection of the 5 per cent. revenue surtax (see paragraph 329 of annual report, 1935) was in June 1936 continued until the 1st July, 1937.
- 267. The Government of India has decided to postpone the enforcement of the land customs régime until the 1st April, 1937, on the administrative separation of Burma. The Government of Burma has not yet decided what additional duties will be imposed (see paragraphs 318–321 of annual report, 1935).
- 268. On the 12th December, 1936, notes were exchanged providing that article 11 of the convention between Great Britain and China relative to Burma of 1894 should, in so far as it related to spirituous liquors, be null and void (see paragraph 322 of annual report, 1935).
- 269. As a matter of grace and in contravention of the Regulations for the Bond Reconditioning Warehouses, the Chinese Maritime Customs are prepared to grant on certain duty-paid articles of foreign origin freedom from interport duty, although the goods are reconditioned and/or repacked locally with Customs supervision after importation.

- 270. In June 1936 the Provisional Regulations for Bonded Manufacturing Warehouses were put into force by the Shanghai Customs for one year as an experimental measure.
- 271. The procedure in connexion with the issue of Chinese consular invoices has been modified and the amendments to the regulations previously in force have been reported to the Foreign Office. They are not such as seriously to affect British trade.
- 272. Written, and informal oral, representations were made to the Waichiaopu in February and March with regard to the exchange of notes on the 2nd and 5th September, 1933, and the declaration of the 4th May, 1935, which were attached to the Sino–Indo-China Convention of 1930, to the effect that His Majesty's Government presumed that, in so far as the origin of importations into China is concerned, there would be no infringement of the most-favoured-nation rights of His Majesty's Government; attention was drawn to the possibility that demands might be made for similar preferential treatment of goods imported from neighbouring territories other than French Indo-China, and also to the fact that differentiation of the tariff based on the regions into which goods are imported is not only contrary to the intentions of the Chinese Government, as declared in annex 4 of the Sino-British Treaty of 1928, but might lead to demands by neighbouring countries other than French Indo-China for similar preferential treatment of goods imported into those regions of China which are contiguous to the territories they control.

IX.—Conservancy.

- 273. The affairs of the Hai Ho Conservancy Commission have progressed satisfactorily and the intervention of this Embassy has not been called for. A demand (possibly instigated by Japanese interests) was made in April for the addition of four more Chinese representatives on the board and for the appointment of a Chinese secretary and a Chinese engineer-in-chief on equal footing with the foreign secretary and the foreign engineer-in-chief. The renewal of the foreign secretary's appointment was used as a lever in an attempt to enforce these demands. The renewal of the latter's appointment was eventually unanimously approved, while at the same time it was agreed to continue the employment of a Chinese secretary (under the foreign secretary) to serve as a liaison officer between the board and the Hopei officials (see paragraph 348 of annual report 1935).
- 274. The affairs of the Chefoo Harbour Improvement Commission have given rise to a voluminous and intricate correspondence, largely in the form of observations by the interested heads of mission whose views on the various questions which have arisen have frequently been diametrically opposed (see paragraph 344 of annual report 1935). It having been ascertained that the Chinese Government had no funds available to finance any major comprehensive scheme of harbour improvement, the commission proceeded to call for tenders for dredgers and other equipment with which to carry on the dredging work urgently necessary in the harbour. The Netherlands Minister objected to this decision on the grounds that the commission was already committed to give the work to the Netherlands Harbour Works Company under the terms of the 1933 "contract."
- 275. The Japanese consul in the course of a violent and offensive correspondence with His Majesty's consul, who was consular representative on the commission, took the stand, in which he was supported by the Japanese Ambassador, that the purchase of dredgers, &c., by the commission was a major work which called for the approval of the Diplomatic Body, and he made allegations to the effect that each and all of the British members of the commission had been guilty of impropriety as a result of which tenders by a British firm had been accepted. None of the points which have come under discussion in connexion with these matters has been settled in principle, but meanwhile the dredgers have been bought and paid for and urgently needed dredging has been proceeded with. This Embassy has maintained the attitude that the Tariff Treaty of 1928 restored to China full liberty of action to impose local ad hoc levies of this kind for conservancy and other purposes in the form of surtaxes on customs duties; and that, in the case of the Chefoo Harbour Improvement Commission, the interested

heads of mission have for the time being no grounds of intervention in connexion with the expenditure of funds by the commission because the commission's funds, though they are derived from surtaxes originally agreed to conditionally by the Diplomatic Body, are entirely at the disposal of the Chinese Government until such time as the loan made in 1918 by the Customs to the commission shall have been repaid.

276. On the 2nd July, 1936, His Majesty's Chargé d'Affaires presented a memorandum to the Waichiaopu requesting that the question of the continued levy of the International Bridge Surtax at Tientsin should be re-examined, and expressing the hope that it might be found feasible to bring it to an end (see paragraph 346 of annual report 1935).

X.—BOXER INDEMNITY.

- 277. During the year the following information was received with regard to the system of re-election of the members of the Board of Trustees of the British section of the Boxer Indemnity Fund:—
- 278. At the first meeting of the board on the 8th April, 1931, it was laid down that the members of the board should be divided into three lots with a term of office of one, two and three years respectively. Lots were drawn to decide the distribution of members with the following result:—

To serve for one year: Messrs. Wang Chia-chen, Soong Tse-liang, W. W. Hornell, R. Calder-Marshall and Chen Tsi-tsai.

To serve for two years: Messrs. Li Shu-hua, K. Cantlie, Yeh Kung-cho, Chen Chung-chun and Tseng Yung-pu.

To serve for three years: Messrs. W. H. Donald, Tseng Yang-pu, N. S. Brown, Huang Han-liang and Chu Chia-hua.

- 279. At the expiration of the terms mentioned above, the members were reappointed for a uniform term of three years. Those appointed for two years were reappointed by the National Government in April 1933 for a further term of three years and again reappointed in April 1936 (with the exception of Mr. Chen Chung-chun, who was replaced by Mr. Li Ssu-kuang (J. S. Li) for a further term of three years.
- 280. In future new members of the board replacing those of the original members who resign before the expiration of their terms will all be appointed for a term of three years.
- 281. In May the board of trustees suggested that a loan should be raised in London on the Boxer Indemnity Funds for the financing of the projected new Chungking-Changsha Railway. No decision had been reached by the end of the year.
- 282. On the 4th August the fourth group of Chinese students sent to study in Great Britain with scholarships granted by the Board of Trustees of the British Indemnity Funds, consisting of nineteen men and one woman, sailed from Shanghai. Prior to sailing, the students were entertained for a week in Nanking, where they received generous hospitality from the British community.
- 283. In connexion with the loans for the construction of the Hsuancheng-Kweichi section of the Nanking-Kiangsi Railway (referred to elsewhere in this report), arrangements have been made whereby amortisation payments on loans already made by the trustees (which are free money that the Chinese Government may spend elsewhere than in the United Kingdom) are utilised to finance further purchases in the United Kingdom.
- 284. The unsuitability of certain locomotives bought through the Boxer Indemnity Purchasing Commission in London has given rise to much correspondence, and the question of the appointment by the Ministry of Railways of a British expert to check specifications is to form the subject of informal representations.

XI.—AVIATION.

285. Further progress has been evident in both civil and military aviation during the year 1936. The celebration of the 50th birthday of Marshal Chiang Kai-shek centred round aviation, in that the generalissimo specified that for birthday gifts he desired only aeroplanes. The intensive campaign which ensued to raise the necessary funds received public acclaim, whilst great enthusiasm was displayed by all classes and the slogan "Salvation by Aviation" became the popular catch phrase of the day.

286. With the appointment of Mme. Chiang Kai-shek as Secretary-General for Air, considerable reorganisation has been effected, not only in the air force but also in the Commission on Aeronautical Affairs itself. In spite of this effort, the annual inspection of the Central Aviation School at Hangehow in October by Marshal and Mme. Chiang exposed a serious lack of discipline and efficiency. Subsequently a full report on the air force was called for from General Silvio Scaroni, the senior foreign air adviser. This report, which was submitted only recently, shows a disturbing state of affairs throughout the service, where incompetence, corruption and inefficiency are stated to run through the organisation from the Commission on Aeronautical Affairs downwards. Active measures are now being taken to rectify this condition and a determined effort is being made under the direct control of Mme. Chiang to raise the air force to a state of efficiency and preparedness for war.

287. With the defection in July of the Kwangtung air forces and their subsequent transfer to the Central Government, an important step towards unification in China was accomplished. The Central Government now has at its disposal an air force consisting of approximately 350 military aircraft and 200 training machines. These figures are inclusive of all reserve aircraft. Kwangsi, which still remains semi-independent, also has a small air force.

Foreign Air Advisers in China.

288. The period under review is noteworthy for the gradual elimination of the Italian and American air advisers and instructors employed by the Central Government. Since the Italian and German rapprochement with Japan, the desire of the Chinese to obtain the assistance of British air advisers has been very evident. Squadron Leader Malley (formerly adviser to the Canton air force) is now being appointed as air adviser to the Commission on Aeronautical Affairs at Nanking. This appointment, coupled with the hardening of Chinese opinion against Italy, will make the position of General Scaroni difficult and his elimination appears imminent. Colonel Reinberg, senior American adviser, died suddenly in November and is not being replaced. The Italian instructors at Loyang have been removed, but some remain at Nanchang whilst certain American technical experts are still employed at Hangchow.

Air Defence Organisation.

289. Air Defence Associations have been formed in most of the large centres particularly vulnerable to air attack. A determined effort is being made to bring home to the general public the dangers to which they are exposed as a result of air attacks. Lectures are given and extensive propaganda has been instituted, whilst several of the larger cities have erected large hoardings in prominent places showing graphically the effect of air bombing. Tentative steps to provide anti-gas instruction have been made and a certain number of gas masks are now available for issue.

Sales of Aircraft.

- 290. Whilst sales of aircraft to China have been confined largely to American and Italian manufacturers, the present trend is towards British aircraft, and tentative enquiries have recently been received for the supply of four British machines. Further and larger orders are expected to result should these initial orders materialise.
- 291. During the first ten months of this year, the Central Government imported 107 aircraft, of which 83 were of American and 24 of Italian manufacture. In addition a large quantity of aircraft parts and engines were imported for the Central Aircraft Factory at Hangehow.

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292. During a similar period, thirty-three aircraft were imported through Canton of which sixteen were of German and seventeen of American manufacture. It is understood that the German aircraft manufacturers have not been paid for the supply of Heinkel and Focke-Wulf machines which have been transferred to the Central Government air force.

Civil Aviation.

General.

- 293. Civil aviation has received much impetus this year with the opening in June of a Civil flying training school at Lunghwa (Shanghai). Foreigners are, however, still debarred from receiving instruction. Thirty-three Chinese, including one girl, completed the six months' course in December. It is anticipated that further schools will be opened shortly in various parts of the country.
- 294. Following extensive trial flights, Imperial Airways inaugurated a weekly air service between Penang and Hong Kong in March, although the Chinese postal authorities would not accept mails for conveyance by this route until October. In November a through air mail service from Shanghai to Europe was established by agreement between the China National Aviation Corporation and Imperial Airways.

Aircraft Factories.

- 295. A steady output has been maintained from the aircraft factory at Hangchow, and the majority of the aircraft presented to Marshal Chiang Kai-shek were constructed there.
- 296. Progress at the Shiukwan aircraft factory has been somewhat hampered on account of flooding, and it was suggested that it should either be pulled down and re-erected at Ying Tak (Kwangtung) or transferred *en bloc* to Hangchow to enlarge the existing plant there. The Central Government, which now administers the factory, have decided, however, that it shall remain at Shiukwan, and the assembly of Vultee and Curtiss Hawk aircraft is proceeding.
- 297. The machinery for the Sino-Italian National Aircraft Works at Nanchang arrived in May and has since been erected but no aircraft have, as yet, been assembled. Signor Acampora is in charge of the factory.
 - 298. The Sino-German factory proposal is still in abeyance.

Far-East Aviation Company.

- 299. The activities of this company have now been divided between the Far-East Flying Training School and the Far-East Aviation Company. During the year, the affairs of the flying training school have prospered and this side of the company is now running at a profit. Pilots of the Hong Kong Volunteer Defence Corps are being trained by the school and the training of Royal Air Force reserve officers is also undertaken. At present there are thirty-three flying students and forty-one engineering students under instruction at the school.
- 300. The aviation side of the company has encountered considerable difficulty during the past year. The troubles in South China, coupled with lack of interest on the part of British manufacturers, has made it almost impossible to push the sale of British equipment.

China National Aviation Corporation.

- 301. Satisfactory progress has been achieved by this company. Passenger fares have been further reduced and all main services have been augmented. One new Douglas D.C.2 aircraft has been acquired but two Ford air liners have been totally destroyed without loss of life.
- 302. On the 5th November Hong Kong was included as a port of call on the Shanghai–Canton route, thus linking up with Imperial Airways' European air service. The proposed Canton–Hanoi service has not been proceeded with as a result of this contract being awarded to the South-Western Aviation Corporation. Owing to lack of traffic, the Kweiyang–Kunming section of the Chungking–Kunming air service has been discontinued.

Eurasia Aviation Corporation.

- 303. Owing to their failure to establish through air communication with Europe, this company's affairs are still unsatisfactory although they are actively searching for a means of overcoming this difficulty. One new Junkers Ju. 52 air liner has been acquired during the year.
- 304. On the 1st April the Sianfu-Chengtu service was extended to Kunming, and since then a regular twice-weekly schedule has been maintained. The company hope eventually to be able to extend this route either to Hanoi or Bangkok so as to obtain a European connexion. Consideration has also been given to extending the Kunming service to Calcutta with a view to linking up with Imperial Airways' route to Europe.

South-Western Aviation Corporation.

- 305. Following attempts by the China National Aviation Corporation to establish a Canton-Hanoi air service, the South-Western Aviation Corporation obtained the approval of the Ministry of Communications and on the 10th July commenced a weekly service to Hanoi, where a connexion is made with the European air service of "Air France."
- 306. Kweilin and Liuchow have recently been added as ports of call on the Canton–Lungchow air route.

Pan-American Airways.

307. After much hesitation whether Macao or Hong Kong should be their Asiatic terminus, Pan-American Airways decided in favour of the latter and, on the 23rd October, the first trial flight from Manila to Hong Kong was made. When the service is finally established between San Francisco and Hong Kong, the colony will become important as the centre of a network of international air services.

Hui Tung Aviation Company.

308. On the 17th November, this company was formed at Tientsin (see paragraph 310) and the following services are now being operated:—

Tientsin-Dairen.

Tientsin-Peiping-Kalgan-Changpei. Tientsin-Peiping-Chengte (Jehol).

Peiping-Tientsin-Shanhaikwan-Chinchow.

Japanese Air Penetration.

- 309. Japanese military aircraft continue to fly with impunity over North China and have gradually extended their flights as far south as Tsingtao and Taiyuan.
- 310. In November the Hui Tung Aviation Company, an erstwhile Sino-Japanese concern, commenced operations in North China with four air services radiating from Tientsin. The Japanese have been greatly perturbed by the establishment of through air services to Europe by the linking of Imperial Airways and the China National Aviation Corporation at Hong Kong. It seems evident that the inauguration of the Hui Tung Company is intended to be only the first step towards further Japanese air penetration to the south; already they are pressing for extensions southward to Shanghai.

Visits by Royal Air Force Units to China.

- 311. In February and March three "Singapore III" flying boats from No. 205 (F.B) Squadron, Singapore, carried out a cruise to China. This flight was the first official visit of the Air Officer Commanding, Royal Air Force, Far East to China. A stop of one week was made at Shanghai, from which place an official visit was paid to Nanking. On the return journey to Singapore a similar visit was paid to Canton.
- 312. In October the aircraft carrier, H.M.S. *Hermes*, visited Shanghai, it being the first time for four years that a ship of this type had visited this port. The opportunity was taken to show a number of the senior officers from the Commission on Aeronautical Affairs over the ship.

British Air Services to China.

- 313. On the 5th November the China National Aviation Company announced the inauguration of a thrice-weekly service from Shanghai to Hong Kong, connecting with the weekly Imperial Airways service to Europe. The establishment of this service followed months of discussion and negotiation, due to the existence of two opposing schools of thought, the one in favour of granting landing rights in Hong Kong to Pan-American Airways and China National Aviation Corporation only on condition of reciprocity—which the Chinese were certain to refuse—the other in favour of effecting a junction with China National Aviation Corporation at all costs before the rival French line based on Hanoi could effect a similar junction and eclipse Hong Kong as Far Eastern air entrepôt. The latter view prevailed, and the Chinese were offered landing rights in Hong Kong without any condition of reciprocity; they were, however, asked, firstly, to promise most-favoured-nation treatment if any foreign service were allowed to operate in China, and, secondly, to give rights of transit across Chinese territory without landing to Imperial Airways aircraft. The first condition was declined by the Waichiaopu, no doubt through fear of the Japanese; as to the second, the Chinese would do no more than promise facilities to planes compelled to make forced landings. In view of the dangers of delay, the claim to most-favoured-nation treatment was abandoned, and on the 2nd September the Government of Hong Kong reported that China National Aviation Corporation had been given authorisation to use Hong Kong, valid for one year, and renewable for four years. Another two months' delay followed before the service actually began to function, due partly to difficulties about the contract, and partly, no doubt, to Japanese pressure.
- 314. The inauguration of the Huitung air service in North China, referred to elsewhere, suggested the possibility of demanding facilities for British aircraft in South China similar to those given to Japanese aircraft in North China. It was made clear to the Chinese Government that His Majesty's Government were watching the situation closely and would expect equal treatment; but it was thought inadvisable to base formal representations on facilities extracted by the Japanese from General Sung Che-yuan under pressure, and not approved by the Central Government. Furthermore, the Chinese might reply that they had refused to promise most-favoured-nation treatment, and that the Huitung Corporation was a Sino-foreign company.
- 315. The Waichiaopu raised objections to the route taken by Imperial Airways between Penang and Hong Kong, alleging that it passed over certain Chinese islands; it was pointed out, in reply, that the route passed between, and not over, these islands.
- 316. Before the inauguration of the Hong Kong-Shanghai service the Chinese Post Office refused to accept air mail marked for conveyance by Imperial Airways from Hong Kong; this difficulty has now been overcome.

XII.—LEGISLATION.

- 317. The Draft Permanent Constitution was promulgated on the 5th May, 1936, for public criticism, with the intention that it should be adopted by the National People's Congress, which was scheduled to open on the 10th November. The congress has, however, been postponed, and action in regard to putting the Constitution into effect has consequently been postponed indefinitely.
- 318. Perhaps the principal piece of legislation issued during the past year is the Income-Tax Ordinance and its detailed enforcement rules, promulgated on the 21st July and the 22nd August respectively, and in force from the 1st October. Actually up to the end of the year income-tax had only been levied on the salaries of Chinese Government employees, including foreigners in Chinese Government service, and it is proposed to levy the tax as from the 1st January, 1937, on the interest of bank deposits and Government bonds and on the profits of business transactions.
- 319. The Insurance Law of the 30th December, 1929, and the Insurance Business Law of the 5th July, 1935, are both at present under revision.
- 320. The Land Law (of the 30th June, 1930) and the Land Law Enforcement Law came into force on the 1st March, 1936. The Land Expropriation Law

of 1928 was repealed as from the 14th March. Active steps are now being taken in different parts of the country beginning in cities and municipalities, for the enforcement of the Land Law by carrying out a cadastral survey and the re-registration of land with a view to the imposition of revised land-tax and the reassessment of land values. At the same time instructions have been issued for a nation-wide geodetic survey to be undertaken. Other land legislation issued comprises, Outline governing the Enforcement of the Procedure of Land Administration in the various Provinces and Municipalities (of the 22nd February), General Principles governing the Levy of Special (Betterment) Fees on Improved Land in Cities and Municipalities (of the 11th April), and Ordinances governing the Payment of Assessment Experts and Title Deed Experts (of the 3rd March).

- 321. The Military Service Law (of the 17th June, 1933) came into force on the 1st March, 1936. Citizen military service is already widely enforced and Government military training is being given to cadets in universities and middle schools, but conscription proper still remains a paper measure, although a beginning is being made of enforcement in certain provinces.
- 322. The smuggling problem formed the subject of various regulations, such as the Provisional Regulations for the Inspection of the Transportation and Sale of Imported Goods and a Provisional Ordinance for the Punishment for Evasions of Customs Duties.
- 323. As regards shipping, the Marine Radio Stations Ordinance (of the 25th March, 1935) governing wireless on ships came into force on the 1st November, 1936. An ordinance was issued on the 9th October providing for subsidies for the encouragement of ship-building, but has not yet been enforced.
- 324. Revised Provisional Ordinances for the Punishment of Narcotics Offences and Opium Offences were promulgated and enforced by the National Government on the 3rd June, 1936. The death penalty is provided for certain categories of narcotics offenders as from the 1st January, 1937, and notices as to this provision were posted at the end of the year in different parts of the country. In order to enforce the control and suppression of opium, Opium Suppression Commissions were set up under the Military Affairs Commission.
- 325. Among miscellaneous legislation issued during the year 1936 may be cited, the Mines Compound Law of the 25th June, the Detailed Rules for the Enforcement of the Provisional Regulations relating to Notaries Public of the 14th February, the Rules governing the Taking of Cinematograph Films by Foreigners in China, which were communicated by the Waichiaopu to His Majesty's Embassy in a letter dated the 7th October, and the Provisional Ordinance for Public Cemeteries of the 30th October. In a somewhat different category are the Emergency Measures for the Maintenance of Public Order promulgated by the National Government on the 20th February.
- 326. Social legislation issued in 1936 includes the Minimum Wage Law, promulgated the 23rd December, and the Labour Contract Law, promulgated the 25th December; both these laws still await mandates fixing the date of enforcement.

XIII.—PROPAGANDA.

- 327. No notable change of policy or increase in activity with regard to propaganda appears to have taken place since the date of last year's annual report.
- 328. Mention, however, should be made of the issue of information bulletins by the Council of International Affairs in Nanking which commenced in May, and to certain plans for the extended use of broadcasting. The Council of International Affairs, although it purports to be entirely unofficial, is in reality controlled by the Waichiaopu. It is, however, independent of the Ministry's Press and Publicity Department, although its director is in close touch with the Minister for Foreign Affairs. Funds for the council's work are provided out of a special allowance of 30,000 dollars a month which the Waichiaopu receives, to be used at the Minister for Foreign Affairs' discretion. The Bulletins which it

issues have been appearing regularly three times a month and are obviously intended to acquaint the foreign public with China's point of view on current topics and with the results of her endeavours in the field of reconstruction.

- 329. As regards broadcasting, regulations were issued in November providing for strict governmental control over all stations and for the broadcasting even by privately-owned stations of a high percentage of Government propaganda. The regulations also stipulate that, with the exception of the amusement items, the "Mandarin" speech must in future be used by broadcast speakers. This stipulation, if enforced, will by its encouragement of the more general use of the Mandarin speech undoubtedly tend to accelerate the cohesion of the various parts of the country where the attitude of the population is now parochial, and, in general, to the consolidation of a national ideal.
- 330. A significant fact in this connexion is the great and growing demand among the poorer classes for earphone sets (for which licences are not required) imported from Japan and costing 2 or 3 dollars each. Even the poorest families living in mat sheds and verging on destitution commonly invest in these. Moreover, it is reported on good authority that the Executive Yuan has issued instructions that at least one loud-speaker radio receiving set must be installed in every hsien within the next six months, and that 146 students (having completed an intensive two months' training course in radio broadcasting and cinematography under the auspices of the Ministry of Education) are about to be despatched to their native provinces in order to popularise broadcasting and educational films.
- 331. In February the Marconi Wireless Company secured a contract from the Chinese Government for the erection of a high-power short-wave station which it is understood is specially required for the purpose of reaching Chinese overseas communities.
- 332. In Shanghai the Chinese Government has continued to carry on its propaganda activities on much the same lines as last year. "General politics" and "Kuomintang principles" are its two main categories. The work in connexion with the distribution of information belonging to the first category is undertaken by the intelligence office of the Shanghai City Government, while the propaganda department of the local Tangpu is responsible for distributing information belonging to the second category.
- 333. In addition to these official propaganda activities, the Chinese authorities have also promoted certain semi-official organs for the purpose of conducting propaganda relative to their respective sphere of activities. The following are the main organisations known to be operating in Shanghai at present:—

The Shanghai Municipality Character Reading Educational Committee.

The object of this committee is to enforce the study of Chinese characters among the illiterate and a knowledge of Kuomintang principles.

The China Aviation Construction League. Shanghai Office.

The New Life Movement Branch of Nanchang Headquarters.

Its duty is to enforce the New Life Movement in Shanghai and conduct propaganda in its favour.

The China Culture Building Society.

This society is more or less a subsidiary organ of the Central Executive Committee of the Kuomintang at Nanking. It publishes every month a periodical containing, in addition to literary and cultural articles, comments on both national and international political situations in China.

334. In March the Chinese authorities ordered that local broadcasting stations should be used exclusively for one hour between 8 p.m. and 9 p.m. during week-days for rebroadcasting the programmes of the Central Broadcasting Station, Nanking. In December the Central Broadcasting Direction Committee of the Central Executive Committee of the Kuomintang established a Shanghai office for the purpose of censoring the programmes of local radio broadcasting stations.

- 335. The number of newspapers, periodicals and news agencies engaged in propaganda on behalf of the Chinese Government remain approximately the same as last year.
- 336. In Canton, following the establishment of the authorities of the Central Government there in the course of the year, new managing directors were appointed to the various official newspapers. The Central News Agency has opened a branch in Canton and now supplies the main part of the political news to the local press. A new agency, called the International News Agency, has been established under the direction of the mayor and will distribute articles in English to the two local English language newspapers.
- 337. In Hankow His Majesty's consul-general reports that no public antiforeign propaganda activities have come to his notice during the past year. On the contrary, so anxious have the Chinese authorities been to avoid incidents involving the Japanese, that instructions have been published repeatedly in the press enjoining the special protection of foreigners. Outspoken leading articles criticising Japan's policy in China have, however, appeared from time to time in the Chinese press.

XIV.—CLAIMS.

- 338. Lists of further claims amounting to 275,112 rupees for losses incurred in the Sinkiang disorders (please see paragraph 299 of annual report for 1935) were received from His Majesty's consul-general at Kashgar and presented to the Waichiaopu on the 23rd April together with a further claim of 26,000 rupees in respect of compensation for the deaths of thirteen British subjects who lost their lives as a result of the aforesaid disturbances. The Waichiaopu replied on the 19th May categorically repudiating liability for the losses incurred, on the grounds that both the Central and Provincial Governments had made every effort to protect foreigners. They added that the payment already made was a voluntary act on the part of the Chinese authorities due to their desire to promote friendly relations between the two Governments.
- 339. As a result of the Waichiaopu's attitude, it was decided that it would be useless to press the Chinese Government further to pay the sum of 275,112 rupees in respect of the losses incurred, but that a further effort should be made to induce them to pay 26,000 rupees in compensation for the deaths of British subjects. Action on these lines was under preparation at the end of the year. All instalments due under the agreement for the repayment of £16,605 0s. 9d. between the Ministry of Communications and three British firms (see paragraph 398 of annual report for 1935) were paid off in the course of the year.
- 340. Commander Davies, who was paid an allowance of 6,000 yen last year by the Japanese Government (please see paragraph 400 of annual report for 1935), died on the 16th January. In answer to an enquiry from the Registrar of His Majesty's Supreme Court at Shanghai, the Japanese consul-general stated that the allowance paid by the Japanese Government to Commander Davies ceased with his death.

Register No.

P. z.7706/36

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POLITICAL DEPARTMENT

Minute Paper.

Dated

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FOR INFORMATION.

This report is rather late in reaching us and much of it is consequently out of date. The marked passages on pages 2-8 dealing with the general internal political situation in Chia Mongolia, Sinkiang and Tibet are however worth reading. Other passages worth glancing at are on pages 16-23, regarding the relations of the Chinese Government with H.M.G., Japan, the U.S.S.R. and Siam. The Financial Secretary maybe interested in pages 38-46 regarding China's currency troubles.

SEEN POLITICAL COMMITTEE

DEC 1936

Military Secretary, Sen Trank Yn. 13 35.11.36
E. & O. Secretary,
Financial Secretary,

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(14921)

CHINA

Annual Report, 1935.

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Mr. Howe to Mr. Eden .- (Received June 2, 1936.)

(No. 420.) Sir,

Sir,

I HAVE the honour to transmit herewith the annual report on China for the year 1935. I am indebted for the preparation of this report to the members of the staff of this Embassy, who have all assisted in its compilation.

I have, &c. R. G. HOWE.

Enclosure.

Annual Report on China for 1935.

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I.—Internal Political Situation.

(1) General.

The outstanding features of the year 1935 in the political situation in China have been a steady improvement in the Communist-bandit situation, the extension of the Central Government's authority in the western provinces, and a closing of the national ranks in face of the ever-growing menace of Japanese aggression. China's relations with Japan have, during the past year, as in the preceding four years, dominated the internal situation and necessarily form the background of any review of political developments and the progress of the Chinese Government.

- 2. During the early part of the year interest was concentrated on the struggle, which continued unabated, between the National Government and the forces of disorder, represented by the so-called Red armies of the Communists. By the end of 1934 the campaign in Fukien and Kiangsi had been concluded, and with the withdrawal of the rebels further west the problem was removed to other theatres and assumed a somewhat different aspect. The main Communist armies theatres and assumed a somewhat different aspect. The main Communist armies were now divided into three groups, one in North-West Hunan, one in Northern Kweichow and Southern Szechuen, and the third in Northern Szechuen and along the borders of Shensi and Kansu. The problem before the generalissimo was to prevent the junction of these forces and particularly to prevent the main forces in the mountains south of the Yangtze from crossing the river and occupying the rich areas of Central Szechuen. To meet the changed conditions the generalissimo in February removed his headquarters from Nanchang to Wuchang, where the "Young Marshal," Chang Hsueh-liang, was placed in charge, while General Chiang himself proceeded to Chungking, where he established a branch of his headquarters, and from there directed in person the operations against the Communists in Szechuen. He took with him to Chungking several divisions of Government troops, thus extending for the first time the military authority of the National Government into that province. Even with this stiffening, however, the local troops of General Liu Hsiang were unable or unwilling to cope effectively with the Communists, but nevertheless the generalissimo succeeded by steady pressure in forcing them westwards into the more inhospitable parts of the province, and though till the end of the year the Communists were free to move in a north-and-south direction from Kansu almost to the confines of Yunnan, they were unable to break eastwards through the military cordon into the fertile plain of Chengtu.
- This was already a signal achievement on the part of the generalissimo, but it was only one part of the task which he had set himself. The other part, the consolidation of the Central Government's authority in the west of China, he set about with equal energy. He cut away with one vigorous sweep the tangled growth of illegal levies and surtaxes collected by the provincial barons for the benefit of their own exchequers, and allowed the stream of trade to flow again between Szechuen and the outer world. With one authoritative word he ended the anti-British boycott which had been in force at Wanhsien since 1926. He built roads. He put life and vitality into everything he touched. In March he paid a visit by air to Kweiyang to direct the operations of the Government forces in the Province of Kweichow, to confer with the local authorities and to reorganise the Provincial Government. The results were remarkable. This province, until recently ruled by its military leaders as a part of the semi-independent south-west. now passed under the more or less direct control of the generalissimo and the Central Government, while missionary reports from Kweiyang described the astonishing changes which came over this remote, old-fashioned and opium-sodden city, with the arrival of the generalissimo, the well-disciplined and relatively efficient Central Government troops and the propagandists of the New Life Movement.
- 4. From Kweichow General Chiang proceeded in due course by air to Yunnan, where likewise his influence and personality did much to strengthen the bonds between this distant province and the Central Government. On his return to Szechuen he did not remain long in Chungking, for before the end of May he was in Chengtu, where he established himself in advanced headquarters on the stopes of the sacred Mount Omei. The move was probably due as much to political as to military considerations, since he was there almost inaccessible to the

Japanese, who now, as a result of recent incidents in North China and other parts of the country (as to which see the section on relations with Japan), were exerting direct and personal pressure on the Chinese Government to arrive at a comprehensive settlement with Japan, and were pressing particularly for the presence in the capital of General Chiang Kai-shek, in order that they might be in a position to deal directly with the *de facto* head of the Central Government.

- At this point Mr. Wang Ching-wei, president of the Executive Yuan and concurrently Minister for Foreign Affairs, retired on sick leave in the early summer, first to Shanghai and then to Tsingtao, where on the 8th August he tendered his resignation. His adherents in the Government, including Mr. Ku Meng-yu, Minister of Railways, and Mr. Chen Kung-po, Minister of Industries, followed suit a few days later. These developments gave rise to great consternation in Nanking, for Mr. Wang, though he appeared at times to be little more than a figurehead in the Government, was actually, in view of his position as political head of the Kuomintang and chief disciple of Dr. Sun Yat-sen, a very important element in the Nanking Administration. In other words, his presence in the National Government at Nanking made it possible for General Chiang Kaishek to claim for his Administration the support of the Kuomintang, which remained in theory the basis of the Government. In this emergency General Chiang flew from Szechuen to Nanking, where Mr. Wang had been persuaded to meet him, and as a result of the discussions which ensued Mr. Wang and his colleagues were persuaded to withdraw their resignations. Though the reasons for this change of mind have never been publicly disclosed, there is little reason to doubt that General Chiang gave an undertaking that he would abandon his attitude of ostentatious aloofness from the political side of the Administration, and would by his personal presence at the capital relieve Mr. Wang of some of the intolerable Japanese pressure. For the moment, however, General Chiang returned to Mount Omei.
- 6. At this point it becomes necessary to say a word about the relations between Nanking and the South-West. The Fifth National Congress of Kuomintang Delegates, which had been postponed the preceding year because of the refusal of the south-western delegates to attend, was summoned for November, and it was urgently necessary that, if by any means possible, the presence of the south-western delegates should be secured in order that the congress might be truly representative of the country and that a united front might be secured on the very critical question of Sino-Japanese relations. There was much coming and going of emissaries, but nothing, it seemed, was likely to alter the determination of the south-western provinces to maintain the semi-independence symbolised by the existence of the South-West Political Council, or to assuage their hostility to General Chiang Kai-shek, who was held responsible for the failure to take effective steps to stem the tide of Japanese aggression. His appeals for the sinking of differences in face of the common threat were met with the reply that the South-West would support him in any measure of resistance, but that so long as Nanking continued its passive policy it must do so alone. On the 9th June Mr. Hu Han-min left Hong Kong for Europe. Since his open breach with General Chiang Kai-shek and his expulsion from the National Government in 1931, he had been, from his refuge in Hong Kong, the principal focus of opposition in South China to the Nanking régime. His withdrawal seemed to be a gesture of defiance and to make almost impossible the object which Nanking sought. Nevertheless, negotiations continued, and eventually the south-western leaders agreed to send delegates to the National Congress at Nanking on the express understanding that they were to act merely as observers and to take no part in the reorganisation of the Central Government. Both Marshal Chen Chi-tang and Marshal Li Tsung-jen, the military satraps of Kwangtung and Kwangsi respectively, insisted that it was essential that General Chiang Kai-shek should come out into the open and commit himself by some step which would prove that he was now going to carry out a policy of resistance to Japan, and upon this being done the South-West would be ready to give him active support.
- 7. The Fifth National Congress of Kuomintang Delegates took place in Nanking from the 13th to the 22nd November and was attended not only by a strong delegation from Kwangtung and Kwangsi, but also by General Feng Yu-hsiang and Yen Hsi-shan and representatives of all other shades of opinion

in the party. When it is considered that in the case of the Fourth Party Congress in 1931 separate congresses had been held at Nanking and Canton, and that the Fifth Congress had previously been twice postponed owing to the impossibility of composing the differences between Nanking and the South-West, there is some justice in President Lin Sen's boast that the present congress was a most remarkable manifestation of the solidarity of the party in face of internal difficulties and external aggression. The outstanding features of the congress were a decision that the National People's Congress should be convoked in 1936 (thus bringing to an end the second or "tutelage" period, and introducing the third or "constitutional" period of Dr. Sun Yat-sen's system), and a speech by General Chiang Kai-shek on foreign relations in which, with obvious reference to the Japanese aggression in North China, which was then at its acutest stage (see paragraph 114), he declared the party's policy as follows: "We shall not forsake peace until there is no hope for peace; we shall not talk lightly of sacrifice until we are driven to the last extremity which makes sacrifice inevitable"; and "We should seek harmonious international relations among nations provided there is no violation of our sovereignty. We should seek economic co-operation based on the principle of equality and reciprocity."

- The National Congress elected the members of the Central Executive and Supervisory Committees for the following term, and at the first plenary session of the new Central Executive Committee, which took place immediately after the close of the National Congress, elections were held to select the personnel of the party and Central Government organs, and subsequently the new Ministers and Vice-Ministers were appointed by the Political Council. Mr. Wang Ching-wei had, in the meantime, become the victim of attempted assassination, and though not killed was so seriously wounded as to render his return to politics most unlikely. His name was retained on the Central Political Council and the Standing Committee of the Central Executive Committee, but it was necessary to fill his place as president of the Executive Yuan, and this post was accepted by General Chiang Kai-shek himself, who was thus at last forced to come out into the open and undertake responsibility for administrative policy and foreign affairs instead of working through Mr. Wang Ching-wei as he had been doing during the past eighteen months. In addition to that post, General Chiang was elected vice-chairman of the Standing Committee of the Central Executive Committee and vice-chairman of the Central Political Council, in addition to his existing post of chairman of the Military Affairs Commission, so that he is in a position to make his weight felt wherever circumstances may demand. On the other hand, he has accepted Mr. Hu Han-min (who is expected back in China towards the end of January) as chairman of the Standing Committee of the Central Executive Committee and Generals Feng Yu-hsiang and Yen Hsi-shan as vice-chairmen of the Military Affairs Commission. On the ability of General Chiang Kai-shek to harmonise these diverse elements will depend the success or failure of the "common front."
- 9. Only four new men were introduced into the Cabinet, and of these two were educated in Japan. Of the twelve major posts in the Government, six, including the Ministries for Foreign Affairs, Interior, War, Industries and Railways, were now held by men who had received their education in Japan, and it would seem that this was done deliberately in order to conciliate Japan and produce an atmosphere favourable for the general discussion of Sino-Japanese problems in regard to which General Chiang Kai-shek had already made overtures to the Japanese Government.
- 10. The détente which General Chiang was seeking to produce was gravely endangered by the activities of the Japanese army in North China and the erection of the puppet "East Hopei Autonomous Council." The apparent supineness of the Central Government in face of these provocations aroused a storm of indignation among the student organisations all over China. As in 1931, railway traffic was interrupted by the invasion of students demanding transport to Nanking for the purpose of laying protests before the Central Government direct. The situation was, however, tactfully handled, General Chiang Kai-shek promising to receive student delegates in Nanking after the new year, and the crisis passed over without provoking the Japanese to retaliatory measures. Mr. Tang Yu-jen, who as Vice-Minister for Foreign Affairs had been closely

associated with Mr. Wang Ching-wei in the earlier Japanese discussions, was assassinated on Christmas Day. This murder and the attempt on Mr. Wang's life are probably intended as warnings to other would-be conciliators, and it remains to be seen whether those members of the Government who have the responsibility of negotiating with Japan have the firmness of mind to reject the hint.

11. The year thus closes on a note of gloom. The dispute with Japan is paralysing all the functions of government. Nothing is worth while doing, very little can be done, so long as every forward move, whether in the political, social or economic field, is liable to be brought to nothing by the simple "No" of a powerful neighbour, and while whole provinces are being torn from the map of China by a military force which is apparently subject to no law or control. Before this menace all else fades into relative unimportance: Communists, floods, currency chaos, financial stringency, breakdown of rural economy—all issues of first magnitude—take second place, and are, indeed, rendered the more intractable by reason of the Japanese menace.

(2) Mongolia.

- 12. There has been little change in the Mongolian situation during the past year. The complex and many-sided struggle for domination between Soviet Russia, Japan, China and—last and probably least—the Mongols themselves has continued unabated.
- 13. The situation as a whole has been dominated by the main conflict between Russia and Japan, each manœuvring to establish a strong defensive position against the other, in view of a possible war. The Soviet Government has to all intents and purposes put a ring fence round Outer Mongolia, which is most jealously guarded against penetration from any quarter, but especially against Japan. The latter strongly resents this exclusion, and has during the past year made a determined effort to break down the barriers. The undelimited frontier between Manchuria and Outer Mongolia gives rise to endless "incidents," in which it is impossible to say which side is the aggressor. One such incident occurred in January at Lake Boir-nor, north of Dolonor. After the usual charges and counter-charges had been exchanged, it was agreed that a conference should be held at Manchuli to settle the dispute. When the conference assembled in May the Manchurian delegates announced that boundary incidents were in themselves trivial matters; the essential thing was that friendly relations should be established between the two territories, and they urged therefore that normal diplomatic relations should be instituted. The Mongolians replied that they had no desire to enter into diplomatic relations with Manchuria, and they refused to be drawn into any discussion on the subject. At this moment another frontier incident occurred and the suggestions now turned to demands which, in accordance with the familiar Japanese technique, were reinforced by threats from the Kwantung army. But the Outer Mongolian Government, with the Soviet behind them, could afford to hold their ground. They rejected the demands out of hand and instructed their delegation at Manchuli to discuss nothing but the frontier This did not suit the Japanese book at all and in November they at length petulantly broke off the abortive negotiations to the accompaniment of threats from the Manchurian Department for Foreign Affairs that the Manchurian Government would henceforth regard Outer Mongolia as a "dangerous and mysterious region" with which they would settle accounts independently and in their own fashion. A further incident occurred on the 19th December at Bulun Dersun in which a Mongolian outpost was attacked by a considerable Japanese force and one officer and two men were killed. Each side, of course, claims that the other was trespassing.
- 14. In Inner Mongolia Japan's problem is an easier one and her efforts have accordingly shown more promise of results. It will be remembered that in April 1934 the Nanking Government had, in an effort to conciliate the Mongols, set up at Pailingmiao a Mongol Local Autonomy Committee with local powers of taxation, and had promised that Chinese infiltration and the reclamation of pasturage lands for farming would be stopped. The Chinese provincial authorities, and especially the chairman of Suiyuan, have looked with great

disfavour on these arrangements and have put every obstacle in the way of their fulfilment. The claim to taxation, in particular, has given rise to constant friction, which has naturally tended to weaken the already somewhat lukewarm attachment of the Mongols of Inner Mongolia to the Chinese connexion and to make them more ready to listen to the blandishments of the Japanese. The latter have continued to dangle before Prince Teh, the secretary-general of the Mongol Autonomy Committee and the outstanding figure in the Mongol Confederacy, the bait of an empire to comprise Hsingan as well as Inner Mongolia if he will allow a Japanese military mission and wireless station to be established in his palace and generally do what he is told. Prince Teh has till the present not yielded to the Japanese importunities, but, failing a more actively sympathetic attitude on the part of the Chinese authorities, it is thought that he will decide to accept the Japanese offer, and then a new "Manchukuo" will be born into the world.

15. The Chinese Central Government have tried to live up to their promise to prevent further encroachment on the pasture lands in Chahar and Suiyuan, but the Mongols, not satisfied with this, claimed that their authority extended right up to the outer line of the Great Wall. The Japanese characteristically decided that it was their duty to see that these claims were enforced. First of all, in the early part of the year, following one of the numerous incidents which occur so conveniently when they are required, the Chinese forces were compelled to withdraw from Eastern Chahar, which was then declared by the Japanese to be a demilitarised zone. Denuded of troops, the area was placed in charge of Chinese gendarmerie. Ten months later the Chinese gendarmerie were directed to withdraw, and when they resisted they were forcibly ejected by a mixed Manchukuo-Mongol force and a Mongol gendarmerie, believed to have been recruited and trained by the Japanese in Hsingan for the purpose, installed in their place. So now Chinese authority in Chahar does not extend beyond the Great Wall, and Japan has a clear corridor connecting the capital of Jehol with the capital of Inner Mongolia.

(3) Sinkiang.

- 16. By the end of the year 1934 the civil wars in Sinkiang had come to an end, and General Sheng Shih-tsai was in control of the whole province except the Yarkand area, where the main Tungan army had established itself. These conditions continued during the whole of the year under review: the Tungans maintained their footing in Yarkand, and though half-hearted negotiations were carried on between their leaders and the Provincial Government, neither side appeared anxious to come to terms.
- 17. General Sheng, though nominally tendering allegiance to the Central Government, owed his military successes largely to the material assistance which he received from the Soviet and, as was remarked in the report for 1934, the province had become economically, if not politically, a Soviet dependency. The Soviet influence in the administration became increasingly more marked during 1935, with a consequent deterioration in the attitude of the local authorities towards British subjects, who seemed to be deliberately singled out for persecution and annoyance. A number of representations were made by His Majesty's Embassy to the Central Government during the year in regard to incidents in which British subjects were concerned, but in fact the Central Government have little or no control over events in this distant province.
- 18. In the late autumn Sir Eric Teichman, Chinese counsellor to His Majesty's Embassy, proceeded overland to Urumchi (Tihua), the provincial capital, to investigate conditions at first hand, but his report has not been received at the time of writing. From Urumchi he proceeded to Kashgar, which he left on the 10th December for India.

(4) Tibet.

19. The search for the reincarnation of the Dalai Lama has continued throughout the year, but without success, and the government has remained in the hands of the Regent and Council.



- 20. The mission under General Huang Mu-sung which had been sent to Lhassa by the Chinese Government, nominally to offer alms and prayers on the death of the Dalai Lama, left Lhassa at the beginning of December 1934, and returned to China via India. The real object of the mission was to obtain from the Tibetan Government an acknowledgment of Chinese suzerainty, and to induce them to place their foreign relations in the hands of the Chinese Government, to accept the appointment of a Chinese Amban in Lhassa and to agree to considerable interference in the internal administration of the country. The mission does not appear to have met with much success, for although the Tibetan Government acknowledged Chinese suzerainty (which they have never denied) and very grudgingly consented to the presence of Nanking Government representatives at Lhassa, they absolutely refused to allow any interference with the internal administration of the country or the conduct of its foreign affairs. For propaganda purposes the Nanking Government seem, nevertheless, to have assumed the compliance of Tibet with their demands, for references have appeared in the Shanghai press to the "provincial" capital at Lhassa, to the establishment of Chinese post offices in Tibet, and to the proposed founding of a school for Tibetan officials in Nanking. General Huang left behind in Lhassa two members of his mission (one of whom died soon after) and also a wireless set with its operators, in order to enable Nanking to keep in touch with Tibetan affairs. Although there is a group of Tibetan officials which is sympathetic to Nanking, it is said that the general feeling is hostile to the attempts of the Chinese Government to reassert its power in Tibet.
- The Panchan (Tashi) Lama's return to Tibet has continued to hang fire owing to his inability to come to terms with the Lhassa Government. The points at issue are: the restoration of the estates which were confiscated when he left Tibet, the troops which he is to be allowed to maintain, and the amount of his contribution to the general military expenditure of the country. These questions have repeatedly been reported to be on the point of settlement, and as often the negotiations have broken down again. Through his representatives at Peking and Nanking the Panchan Lama has kept in touch with His Majesty's Embassy whose assistance he has invoked with a view to securing a settlement of his differences with the Tibetan Government. In reply he has been informed that His Majesty's Government in the United Kingdom would be very glad to see a settlement of these differences and would avail themselves of any opportunity that was offered to assist the negotiations, but that he would be well advised to moderate his demands and be satisfied if he received the status and possessions which he enjoyed before his flight. At the date of writing this report he is still at the monastery of Kumbum in Chinghai, but is believed to intend setting out on the long overland journey to Tibet as soon as the preparations for the road are complete and without awaiting a complete agreement with the Lhassa authorities. A party of three hundred Tibetans has come from his native Shigatse to welcome him, and the Chinese Government, in addition to providing a sum of 400,000 dollars for travelling expenses, has sent a Chinese Commissioner and an escort of 300 men to accompany him on the journey.
- 22. The decision of the Chinese Government to send this escort caused considerable uneasiness at Lhassa where it was regarded as the forerunner of a fresh Chinese military occupation, and Mr. Williamson, British Resident in Sikkim, who was in Lhassa in October at the invitation of the Tibetan Government, was earnestly entreated to move His Majesty's Government to intervene in the matter. Strong representations based on article 3 of the Simla Convention were accordingly made in Nanking by His Majesty's Ambassador, but it is still uncertain whether they have proved effective. The Chinese have done all in their power to secure the Panchan Lama's favour while he has been in China, and they are now anxious to take the utmost advantage of his return to Tibet to re-establish their temporal power in the country. An armed guard of 300 men may seem paltry enough to European eyes, but in the eyes of the Tibetans it looms as large as an army corps, and there can be little doubt that its presence at Lhassa or Shigatse would considerably enhance the prestige of the Nanking Government in the country.
- 23. It is deeply to be regretted that Mr. Williamson died at Lhassa during the visit to which reference has been made.

Contrary

24. On the Szechuen-Tibetan border the year has passed without any major incidents. The behaviour of the Chinese XXIVth Army in Sikang to the Tibetans on the frontier is, however, said to have been oppressive in the extreme, and there is always a danger of reprisals and incidents.

(5) Military Operations, 1935.

25. During the period under reference military operations have been restricted to the suppression of Communists and bandits in various provinces in China, and a minor clash between Chinese and Japanese troops in South-East Chahar.

Operations against Communists.

- 26. Towards the latter part of 1934 the Chinese "Reds" were occupying large areas in South-West Fukien and South-East Kiangsi, North Szechuan, North-West Hunan, and North Shensi.
- 27. By the end of November 1935 Government and provincial troops had succeeded in driving the formidable Communist forces from out of Fukien and Kiangsi into the north-west corner of Szechuan; compelling the strong body of Communists, which for many years past had been in occupation of the northern districts of Szechuan, to withdraw westwards to the north-west corner of Szechuan and South-East Kansu; whilst energetic steps had been taken with a view to dealing with the Communist menace in North Shensi. Little success could be recorded against the Communists in North-West Hunan until the latter part of November, when the Communists commenced a general withdrawal towards West Central Hunan, from their strongholds in the Tayung-Sanchih area (North-West Hunan). As yet it is too early to predict the outcome of this movement.
- 28. Credit for what has been accomplished must be given to General Chiang Kai-shek. In the first instance he directed operations from his headquarters at Nanchang in Kiangsi, but once assured of the success of his campaign in Kiangsi and Fukien, he visited in turn Kweiyang, the capital of Kweichow, Kunming, the capital of Yunnan, and, finally, established his provisional headquarters at Chungking in Szechuan, from which place he has directed the operations that have successfully penned the main Communist forces within the areas that they occupy at present in North-West Szechuan and North Shensi. All Chiang Kaishek's movements have been carried out by aeroplane, and by this means he has been enabled to co-ordinate the movements and dispositions of the Government and provincial forces, and stimulate and encourage his subordinate commanders whenever the situation had turned in favour of the Communists.
- 29. In addition, he has taken the opportunity of strengthening his hold over the provinces from which the Communists have been expelled or passed through. This applies to Kiangsi, Fukien, Kweichow, Yunnan and particularly Szechuan, a province that for many years past had owed little other than lip service to the National Government at Nanking.
 - 30. The Communist campaign may be divided into four phases:-
 - (a) The expulsion of the forces under Chu Teh and Mao Tze-tung from Fukien and Kiangsi.
 - (b) The successful campaign against the forces under Hsu Hsiang-chien in North Szechuan.
 - (c) The operations against the forces under Liu Tze-tan and Hsu Hai-tung in North Shensi.
 - (d) The somewhat nugatory operations against Ho Lung and Hsiao Ko in North-West Hunan.

(a) The Campaign against Chu Teh and Mao Tze-tung.

31. To deal with this situation Chiang Kai-shek enlisted the aid of Kwangtung and Kwangsi. By the middle of 1934 he had perfected his plans and collected together four armies whose total strength was somewhere in the region of 350-400,000.

- 32. Adopting a converging attack from the north, south, east and northwest, it was not long before the Communist forces, estimated at 80–100,000 strong, began to feel a pressure that was overwhelming and could not be gainsaid.
- 33. By November 1934 the last remaining Communist strongholds (including Juichin, the so-called "Red" capital) in Fukien and Kiangsi were in the possession of Government troops, and this brought about a general dispersion of the Communist forces.
- 34. Small bands, which have since been dealt with, moved towards Anhwei and Chekiang, whilst the main body began a westerly withdrawal along the Hunan-Kwangtung-Kwangsi borders. After seven years of occupation by the Reds, the Provinces of Fukien and Kiangsi passed back to the control of the Nanking Government.
- 35. Prevented from breaking towards the north or south, and pressed from the rear by Government troops, the Communists were shepherded into Eastern Kweichow.
- 36 During the first four months of 1935 they succeeded in crossing Kweichow from east to west, broke into South Szechuan, doubled back on their tracks, and after threatening Kweiyang, the capital of Kweichow, by the end of April, had penetrated into North-East Yunnan and were threatening Kunming, the capital.
- 37. Stimulated by the appearance of Chiang Kai-shek in person and assisted by Government and Kwangsi troops, the provincial authorities of Kweichow and Yunnan were successful in withstanding the Communist onslaughts. The Communist forces, much to the relief of the Yunnan authorities, then swung northwards and succeeded in crossing the Upper Yangtze in the vicinity of Yuanmow. Proceeding northwards via Hweili and Sichang in South-West Szechuan, they succeeded in crossing the Ta Tu-ho (river), and by the middle of June had reached Mowkung in West Szechuan, where they established contact with the Communist forces under Hsu Hsiang-chien.
- 38. For some weeks after this little activity was displayed by either side. This was due to climatic conditions, the fact that both sides were exhausted, and the necessity of reorganising the provincial forces of Szechuan, which were now co-operating with the Government troops.
- 39. During this period of inactivity, General Chiang Kai-shek, who by this time was personally directing operations from Chungking, concentrated on road construction, the building of a blockhouse system, the massing of supplies and the training of his troops.
 - 40. By the middle of July Chiang had completed his new dispositions.
- 41. With a view to preventing the Communists from breaking into South-West Shensi, the 1st Central Government Division had moved from South-East Kansu to the area Sungpan-Kiangyu in North-West Szechuan. Six Szechuan route armies were hemming in the Communists from the east, whilst four armies of Central Government troops, based on Yachow (Yaan), were operating northwards.
- 42. Mowkung was abandoned by the Communists on the 20th July, and a general northward movement towards South Kansu followed. Sungpan was fiercely attacked, but successfully held by the 1st Central Government Division. Skirting Sungpan to the west, by the latter part of August, the Communist vanguards had trickled over the South Kansu border, and by the middle of September a portion under Mao Tze-tung had overrun the southernmost districts of Kansu with Minhsien as the focal point. Lanchow, the capital of Kansu, was threatened, and for a short time communications between that place and Sian, the capital of Shensi, were interrupted.
- 43. The 7th and 12th Central Government Divisions were hurried to the scene and given the rôle of protecting Lanchow. A large number of foreign missionaries, who by this time had collected at Lanchow, were successfully evacuated by raft down the Yellow River to the railhead at Paotow in Suiyuan.

- 44. During November the Communist bands under Mao Tze-tung moved north-eastwards from Minhsien and succeeded in joining forces with Liu Tze-tan and Hsu Hai-tung in the vicinity of Wuchichen and Chingtingshan in West Central Shensi. Since then little news has been received of the movements of this band. In the meantime, Chu Teh appears to have thrown in his lot with Hsu Hsiang-chien in North-West Szechuan.
- 45. It is not yet clear why these two redoubtable leaders have split up. Chinese reports suggest that the separation was due to a quarrel regarding policy and future plans.
- 46. It is interesting to note that, since evacuating Fukien and Kiangsi Provinces in November 1934, the Communists under Chu Teh and Mao Tze-tung have traversed well over 2,000 miles. There is little doubt that their numbers have been sadly depleted during this amazing performance. In actual fighting strength it is questionable whether their numbers at the present time exceed 20–30,000.
- (b) The Campaign against Hsu Hsiang-chien in North Szechuan.
- 47. At the end of 1934 large bands of Communists, with an estimated fighting strength of 40–50,000, were in occupation of vast tracts in North Szechuan. This area extended from Chengkow in the east to Kwangyuan in the west, and from Nankiang in the north to Suiting (Tahsien) in the south. The provincial troops, who were little more than bandits themselves, were quite incapable of dealing with this situation, let alone with threatened "Red" incursions from Kweichow.
- 48. This caused General Liu Hsiang, the chairman of Szechuan, to appeal to Nanking for aid. The indefatigable General Chiang Kai-shek despatched a military mission from his headquarters at Nanchang in Kiangsi to Chungking in Szechuan, with orders to reorganise the military dispositions in Szechuan and assist in the anti-Communist campaign. This mission was backed up by the despatch to Szechuan of Government troops and later by General Chiang himself.
- 49. By February considerable progress had been made by Government and provincial troops, and the Communists began to withdraw in a west and north-westerly direction. One portion penetrated in to South-West Shensi and occupied Ningkiang, where two British missionaries were captured, but subsequently released. In the middle of this month Nankiang and Tungkiang (North Szechuan), two of the most important Communist strongholds, were occupied by Government forces. A drive against the Communists in South-West Shensi caused them to break back again into North Szechuan, where they were successful in reoccupying most of their former territory. This caused General Chiang to fly to Chungking in order to appraise the situation.
- 50. As a result of his activities the main Communist body began to move westwards, and during March fierce fighting occurred in the vicinity of Kwangyuan on the Kialing River.
- 51. Towards the end of March the Communists succeeded in crossing the Kialing River in the vicinity of Tsangki and then moved westwards on Kienko, an important strategic point on the Chengtu-Chaohua highway. Kiangyu was attacked, but without success; and by the middle of May Mowhsien had fallen into their hands. As a result of these successes, Chengtu, the capital of Szechuan, was threatened. Martial law was declared, and most of the missionaries were evacuated. Whilst the main body threatened Chengtu, small detachments began to work their way northwards along the Sungpan River basin.
- 52. It was now evident that Hsu Hsiang-chien's main objective was tolink up with the Communists under Chu Teh and Mao Tse-tung, who at this time were busy crossing the Ta Tu River in South-West Szechuan. This was successfully accomplished by the end of June, contact being effected in the vicinity of Mowkung.
- 53. However, General Chiang Kai-shek had the situation well in hand, and from now onwards his military dispositions in North-West Szechuan were equally directed against the combined forces of Chu Teh, Mao Tze-tung and Hsu Hsiang-chien.

- 54. In July a general withdrawal northwards commenced. Mowhsien was abandoned by Hsu Hsiang-chien, and during the following weeks fierce fighting took place in the area to the south and west of Sungpan. Foiled in their attempts to enter South Kansu and East Tsinghai, Hsu Hsiang-chien and Chu Teh turned south-westwards and made for the Szechuan–Hsikang border.
- 55. In October Tanpa, on the Hsikang border, was captured, and in the middle of November an advance was made on Kantze in Hsikang and Tienchuan and Mowkung in Szechuan. By the middle of the month Yaan, an important town to the south-east of Chengtu, had fallen into the hands of the Communists. This move not only constituted a threat to Chengtu, but threatened a break-away southwards towards Yunnan.
- 56. Under-direct instructions from General Chiang Kai-shek, Government and provincial troops were rushed to the threatened area. During December the Government forces were successful in stabilising the situation; and, according to reports received at the end of the month, it appears that the Communists have been driven north-westwards towards Tienchuan, in which area they are at present.

(c) The Campaign against Liu Tze-tan in North Shensi.

- 57. It was not until the end of May that this band of Communists, estimated strength 8–10,000, under Liu Tze-tan came before the public eye. The Communist situation in North Shensi dates back many years. Of late little has been done to suppress them, but with the main Communist forces in Szechuan threatening to move into Kansu and South Shensi, the situation began to assume acute proportions, and since then rigorous steps have been taken with a view to dealing with the matter.
- 58. The Communists were occupying a large tract of land from Yenchang in the east to Paoan in the west, with Fushih (Yenanfu) as the focal point. In August orders were issued for two Shansi divisions to concentrate in the area Chingchien-Yenchuan (North-East Shensi). Ninghsia troops, under the command of Ma Hung-kuei, moved to the area Tingpien-Anpien-Chinpien (all in North-West Shensi), whilst Kansu troops under Chu Shao-liang were moved to the North-East Kansu border. During August and September the LIst, LVIIth and LXVIIth Armies, all units of the old North-Eastern Army, were moved into Shensi, ostensibly for Communist suppression duties, whilst provisional headquarters were established at Sian with General Chang Hsueh-liang as Deputy Commander-in-chief.
- 59. In July a band of Communists, estimated strength 5,000, under a certain Hsu Hai-tung, began to move from the vicinity of Lonan and Shanghsien in South-East Shensi towards South Kansu. It was expected that they would endeavour to join hands with the main Communist forces in North Szechuan, but in actual fact they broke northwards and succeeded during September in joining up with Liu Tze-tan in the vicinity of Yenchang.
- 60. In the middle of August Liu Tze-tan made an unsuccessful attempt to invest Suiteh (North-East Shensi). The LXVIIth Army (Government troops) began to move northwards on Fushih, whilst the LIst Army was diverted towards the South-East Kansu border in order to watch the movements of Mao Tze-tung, who by this time had filtered into South-East Kansu from North Szechuan. The LVIIth Army was now concentrated at Hsienyang, a large town to the northwest of Sian. By the middle of September the LXVIIth Army had occupied the important town of Fushih, whilst the Communists under Hsu Hai-tung withdrew northwards to Anchai. In the far north of the province the Communists under Liu Tze-tan penetrated into South Suiyuan. A clash with Mongol cavalry ensued, and units of the XXXVth Army (Suiyuan) were rushed to the Suiyuan-Shensi border in order to stabilise the situation. Towards the end of September serious fighting took place in the Chingchien-Yenchang sector.
- 61. During October Government forces received a serious set-back. The 110th Division of the LXVIIth Army was surrounded at Kanchuan (South of Fushih), and according to reports was practically annihilated. Three regimental commanders were killed, whilst the divisional commander is reported to have committed suicide.

- 62. In November the Communists under Mao Tze-tung (from North-West Szechuan) were successful in joining hands with Liu Tze-tan and Hsu Hai-tung in West-Central Shensi. Since then the situation has remained quiescent.
- (d) The Campaign against Ho Lung and Hsiao Ko in North-West Hunan.
- 63. In September 1934 the Communists, estimated strength 8,000–10,000, under Hsiao Ko, crossed the Kiangsi–Hunan border, and during October succeeded in joining hands with those under Ho Lung in the vicinity of Tungjen in Eastern Kweichow. This led to the capture of five missionaries at Laohuangping, a town some 80 miles east of Kweiyang. The ladies, three in number, were released after a few days. After protracted negotiations extending over one year, the Communists in November 1935 released one of their two remaining captives, a Mr. Hayman, of British extraction. Mr. Bosshardt, a Swiss, is still in their hands, and serious doubts are entertained regarding his safety.
- 64. By December 1934 the combined Communist forces, estimated strength 20,000, had moved into North-West Hunan. Taoyuan fell into their hands, and for weeks Changteh, an important city to the north-west of Changsha, was seriously threatened. Government forces under Hsu Yuan-chuan and provincial troops under Ho Chien, the chairman of Hunan, succeeded in stemming the Communist tide; and by the end of March, as the result of a converging attack, the Communists were forced westwards into the mountainous region adjacent to the Hupeh-Hunan-Szechuan borders. During the following months sporadic fighting took place between the Communists and Government troops. In May one Government division was very badly handled, and the Communists again moved eastwards and reoccupied the country as far east as Lichow. Without serious interference they again withdrew westwards, and by the end of June were located along the three provincial borders with Lungshan (Hunan-Hupeh border) as their focal point. By this time it was reported that their numbers had increased to 50,000.
- 65. In the meantime no less than six Government divisions from Kiangsi, Central Hupeh and Anhwei, had been ordered to proceed to South-West Hupeh and North Hunan.
- 66. During the early part of September the Communists were very active. Changteh was again threatened, and at one time it appeared that the Communists were thinking of attempting to cross the Yangtze River between Shasi and Ichang, with the intention of breaking into East Szechuan. The arrival of Government reinforcements restored the situation, and the Communists were again driven back to their old stamping grounds in the vicinity of Tayung, Sangchih and Hofeng (Hupeh-Hunan border).
- 67. Towards the end of the month, under instructions from General Chiang Kai-shek, provisional military headquarters were opened at Ichang on the Yangtze River under the direction of General Chen Cheng, formerly commander of the 3rd Route Army in Kiangsi. To General Chen was given the responsibility of co-ordinating the future movements and dispositions of both Central Government and Hunan provincial troops. In the past, lack of co-ordination has been responsible for most of the disasters that have befallen the anti-Communist forces in this area.
- 68. This new threat had the desired effect. During the latter part of November the main Communist body began a general withdrawal from their strongholds in the Tayung-Sangchih area. Crossing the formidable Yuan Kiang (River), they overran the whole of West Central Hunan, and were evidently attempting to break into Kweichow. Reports received during December indicate that fierce fighting has taken place in the vicinity of Süpu. Government reinforcements have been despatched to the scene of operations, and two Kwangsi divisions have been detailed to the Kwangsi-Hunan border.

(e) Operations in Eastern Chahar.

69. The only clash with foreign troops occurred in the vicinity of Kuyuan in East Chahar between troops of the Chinese XXIXth Army under Sung Che-yuan and Japanese and "Manchukuo" troops. The dispute was in connexion with a few villages that lie in the area to the east of Kuyuan and

Tushihkou. The Chinese claimed that this "hsien" was part of the prefecture of Kuyuan, whilst "Manchukuo" affirmed that it was part of the Fengning (Jehol) prefecture.

- 70. The Japanese military authorities entered into the fray, and on the 22nd January fighting took place between the Chinese and troops of the 7th Japanese Division, in which the Japanese sustained a few casualties.
- 71. This led to further reprisals. The Japanese during the following days bombed from the air and shelled with artillery the villages of Tungchutze and Tushihkou.
- 72. This broke the Chinese resistance. A conference was held at Tatan in East Jehol, and a verbal agreement arrived at by which the area east of a line drawn from Tushihkou to Kuyuan passed within the jurisdiction of "Manchukuo."

(6) Piracy.

- 73. On the 29th January Messrs. Butterfield and Swire's steamship *Tungchow* sailed from Shanghai for Chefoo and Tientsin, and was pirated immediately after leaving the entrance to the Yangtze, some dozen pirates gaining control of the ship by climbing outside the anti-pirate grills on to the deck above and overpowering the Russian guards. One Russian guard was killed and another wounded, and Mr. Macdonald, the second engineer, was also wounded.
- 74. The pirates ordered the ship to proceed to Honghai Bay, 70 miles to the eastward of Hong Kong, disguising her to represent a Japanese steamer, the *Toyo Maru*, by painting this name on the bows and the appropriate markings on the funnel. The ship was carrying some seventy school-children, whom the pirates appear to have treated as well as could be expected. The Chinese passengers, however, were systematically robbed.
- 75. On the 1st February the pirates captured a junk, to which they transferred the loot, some 4,000 dollars in cash and some miscellaneous cargo. The next day the pirates remaining on board the *Tungchow* became alarmed by the appearance of an aeroplane from His Majesty's ship *Hermes* and left the ship in one of the *Tungchow's* boats, taking with them the first officer and the Chinese wireless operator, whom they threatened to shoot in the event of their being attacked. Neither this aeroplane nor two others which subsequently flew over the *Tungchow* recognised her in her disguise. Later, the first officer and the wireless operator returned to the *Tungchow* in the ship's boat, the pirates having made good their escape without taking hostages. The *Tungchow* then proceeded to Junk Bay, where she was met by His Majesty's ship *Dainty* and escorted to Hong Kong.
- 76. Representations by this Embassy to the Waichiaopu led to energetic action being taken by the Chinese military authorities resulting in the capture of four of the pirates.
- 77. The general conclusions reached at the enquiry into the piracy held at Shanghai were that, from the construction and arrangement of the ship, it was not possible, with the number of guards carried, to defend her against the attack, which was well planned. Messrs. Butterfield and Swire have consequently decided to make certain structural alterations in their ships plying on this service, and to strengthen the armed guards by 50 per cent. They have also arranged for all deck passengers to be examined and searched in future before every sailing.
- 78. Following the enquiry into the *Tungchow* piracy, the Chinese Government agreed to the proposal of His Majesty's Ambassador that vessels of the Chinese Maritime Customs Service should co-operate with the coastguard service and the Chinese navy and the British navy in the suppression of piracy. This agreement was subsequently supplemented by an arrangement between the Commander-in-chief of the China Station and the Inspectorate-General of the Chinese Customs, whereby the latter agreed to issue instructions to the vessels and stations of the Chinese Maritime Customs with a view to ensuring full co-operation with the Royal Navy in the matter.

(7) Banditry.

- 79. On the 28th July Mr. Gareth Jones, together with Dr. Müller, a German newspaper correspondent, was captured by bandits in Outer Mongolia while motoring from Dolonor to Kalgan, at a place called Kuanmakou, or Makoutsun. On the 30th July Dr. Müller was released by the bandits for the purpose of negotiating a ransom with the Chinese authorities for Mr. Jones's release.
- 80. Immediately on receipt of the news of Mr. Jones's capture, the Chinese Government was requested by His Majesty's Ambassador to take speedy and effective steps for his early release. Lieutenant Millar, a language officer at this Embassy, was sent at once to Kalgan to take such action locally as might be possible to effect his release and, in addition, close touch was maintained by this Embassy with the Japanese Embassy in case the bandits should cross into Jehol.
- 81. The original demand of the bandits was for 100,000 dollars and arms and ammunition, which was later reduced to 50,000 dollars, and some days later again raised to the original sum. At all times the Chinese authorities expressed willingness to pay any ransom within reason, and gave repeated assurances of their conviction that Mr. Jones's life was not in danger and that it was only a question of time before he would be released. During the course of the negotiations the bandits kept moving and at one period proceeded a short distance into Jehol. Later, when they split into two bands, the Chinese authorities decided to surround one of the bands, the other having proceeded too close to the Jehol border for them to take action. The next development was that on the 16th August Lieutenant Millar received a report that a foreigner had been shot by bandits in the Paochang area, and it later transpired that this foreigner was Mr. Gareth Jones, who, after fifteen days of captivity, had been shot to death by the bandits on the 12th August.
- 82. Immediately on receipt of this information His Majesty's Ambassador made representations to the Chinese Government pressing for a full enquiry and for the arrest and punishment of the murderers. He was subsequently informed that the Chinese authorities in Chahar had several times attacked the bandits, with the result that all but a few had been killed. Unfortunately, no bandits were captured and, so far, no facts have been brought to light to show that there is any foundation for suggestions, based on the mysterious circumstances of the murder, that Mr. Jones's capture was no ordinary case of kidnapping, but involved considerations of a political nature. It is unlikely that any new facts of importance will now emerge.
- 83. The area where the capture and murder took place (the new demilitarised zone between Jehol and Chahar) is a very disturbed one, and Mr. Jones, when he called at the Embassy on the 9th July, was warned to keep away from it. In addition Mr. Jones, Dr. Müller and the third member of the party, Baron von Plessen of the German Embassy at Peking (who returned to Peking before the incident), signed the usual undertaking in Chinese to the effect that they were proceeding outside the Great Wall at their own risk.
- 84. At the end of February reports were received by His Majesty's Embassy that Mr. S. C. Frencham, an Australian missionary stationed at Nankiang in South Shensi, and Mrs. Frencham had been captured by Communists. Urgent representations were immediately made to the authorities at Hankow, to the Waichiaopu and to General Chiang Kai-shek personally to take immediate steps to effect their release, and Mr. Stockley, of His Majesty's consulate-general at Hankow, was sent by aeroplane to Hsian to keep in touch with the Shensi Provincial Government. At the beginning of March reports were received that Mr. and Mrs. Frencham had been killed. At the end of March, however, the China Inland Mission at Shanghai unexpectedly received a telegram announcing the safe arrival of Mr. and Mrs. Frencham at Hangchung, having spent over a month in the hands of the Communists, by whom they appear to be well treated. It is possible that their release was due to the intervention of General Sun Wei-ju, the commander of the Government forces in South Shensi, who is supposed to have reached some sort of unofficial agreement with his Communist opponents.
- 85. In the course of the year unremitting pressure was brought to bear on the Hunan provincial authorities by His Majesty's consul at Changsha and on the Central Government at Nanking by this Embassy to provide funds and

facilities to secure the release of Mr. Hayman, a British subject, and M. Bosshardt, a Swiss national, by the Communists who captured them at the end of last year (see paragraph 62 of the annual report for 1934). The actual negotiations with the Communists were conducted by Mr. Becker, a German missionary of the China Inland Mission. The ransom for the release of both men agreed to by the Communists (10,000 dollars) was finally produced by the Chinese provincial and military authorities at the end of October, and Mr. Becker, after a most difficult and dangerous journey, handed this sum over to the Communists on the 17th November. The Communists, however, broke faith, with the result that only Mr. Hayman was released, a further 10,000 dollars being demanded for the release of M. Bosshardt. The release of Mr. Hayman in preference to M. Bosshardt appears to have been effected entirely on the initiative of the Communists, who feared that the former might die owing to his weak condition. The negotiations had at all times been conducted on the basis of the release of both men. At the time of writing Mr. Becker is engaged in trying to re-establish contact with the Communists for the purpose of arranging for M. Bosshardt's release, and on instructions from the Foreign Office His Majesty's consul at Changsha is also continuing his efforts on M. Bosshardt's behalf.

- 86. At 10·40 p.m. on the 15th August the Peking–Mukden mail train was bandited about half a mile south of Shanhaikuan, the bandits confining their attention to a third-class coach containing Koreans who were known to be carrying notes. After robbing the Koreans, the bandits left the train, which was only delayed about two hours. A train sub-inspector, a railway guard and a Korean were killed and about thirty Koreans wounded.
- 87. Provisional measures drawn up by the chairman of the Military Affairs Commission for the trial of cases of banditry and brigandage during the period of bandit suppression operations now in active progress were approved and placed on record by the Central Political Council at its 471st meeting on the 21st August, 1935, and similar action taken by the National Government was published in the National Government Gazette of the 3rd September. This action has apparently been taken at the instigation of General Chiang Kai-shek, who considered the relevant provisions of the new Criminal Code to be too lenient and the ordinary legal procedure to be too slow and cumbersome.

(8) Revolt of Chinese Cruisers Haichi and Haishen.

88. On the night of the 15th June, owing apparently to some grievance in connexion with their pay, the officers and crew of the ex-northern Chinese cruisers Haichi and Haishen, which since 1933 had been affiliated to the Cantonese navy, revolted and took their ships out of Canton. After an engagement with the Chinese forts on the Canton River, the vessels arrived in Hong Kong for coaling, declaring their intention to obey the instructions of the Central Govern-The Canton authorities approached His Majesty's consul-general and requested that the vessels might be regarded as rebels and interned at Hong Kong, and were referred by Mr. Phillips to the Central Government and to this Embassy. His Majesty's Ambassador adopted the attitude that the vessels should be treated as normal units of the Chinese navy unless and until this Embassy was otherwise advised by the Central Government. The attitude of the Central Government, however, remained ambiguous throughout the incident. After first being informed by the Minister for Foreign Affairs that the vessels intended to revert to the allegiance of the Central Government, His Majesty's Embassy were approached privately by the Waichiaopu with an enquiry as to whether it might not be possible for the Hong Kong authorities to intimate to the commanders of the cruisers that they should leave the waters of the colony. Yet when the vessels did sail on the 21st June they were fired on by the Chinese cruiser Ninghai, sent by the central authorities under the command of Admiral Chen Chi-liang to negotiate with the rebels, and forced to return to Hong Kong. The affair was eventually settled, after negotiations between Admiral Chen and the rebels in Hong Kong, by the return of the Haichi and the Haishen to the Nanking fold. They have, however, been placed under the orders of the chairman of the Military Affairs Commission (General Chiang Kai-shek) and not directly under the Ministry of the Navy.

II.—Foreign Relations.

(A) British Empire.

(1) United Kingdom.

- 89. On the 18th May His Majesty's Government in the United Kingdom announced that they proposed to raise the status of His Majesty's Legation in China to that of an Embassy. This step was taken following information communicated to His Majesty's Ambassador at Tokyo by the Japanese Minister for Foreign Affairs that the Japanese Government proposed to raise the status of their Legation in China to that of an Embassy, and the announcement in respect of both Legations was made simultaneously, after His Majesty's Government had informed the French and United States Governments of their decision. The Chinese Government announced on the same day that they would take similar action with regard to the Chinese Legation in London. On the 23rd May His Majesty the King approved the appointment of His Majesty's Minister to be His Majesty's Ambassador in China, and Sir Alexander Cadogan presented his credentials to the President of the Chinese Republic at Nanking in his new capacity on the 15th June.
- 90. In the middle of June His Majesty's Ambassador was informed by the Foreign Office that a definite decision had been reached to transfer His Majesty's Embassy at Peking to Nanking, while retaining the present accommodation in Peking. On instructions from the Foreign Office, His Majesty's Ambassador informed the Chinese Government of the decision of His Majesty's Government, and up to the time of writing he has been in negotiation with them for the purchase of a site at Nanking suitable for the erection of an Embassy. Difficulty has been experienced in this connexion owing to the claims of the Chinese military on the best sites, but in November His Majesty's Ambassador recommended the purchase by His Majesty's Government of a site which he considered to be the most suitable available.
- In the course of the year His Majesty's Ambassador was asked by the Foreign Office to furnish his views as to whether for the purpose of demonstrating the continuous interest of His Majesty's Government in the United Kingdom in the Far East and their determination to maintain that interest, it would be useful (i) to construct, like the Japanese and French, permanent barracks in Shanghai capable of accommodating strong reinforcements to the present British force, and (2) to increase the British air strength at Hong Kong. As regards the first proposal His Majesty's Ambassador expressed the opinion that under existing conditions British prestige would be enhanced by the construction of permanent barracks. He thought, however, that a better solution would be the withdrawal of all foreign military forces from Shanghai, and that this might be proposed to the Powers concerned. If the Japanese refused, as they probably would, their refusal would furnish additional justification for the construction of permanent barracks for the British forces. His Majesty's Ambassador added that it seemed to him that the Far Eastern military establishment of His Majesty's Government should be concentrated as far as possible in Hong Kong. and as regards the second proposal, therefore, he considered that an increase in the British air strength there would have a good effect on the general situation. His Majesty's Ambassador at Tokyo expressed the opinion that neither of the two proposals if adopted need affect Anglo-Japanese relations adversely provided undue publicity was not given to them.
- 92. The contract for the appointment of Commander A. V. Morse to be head of the British Naval Mission to China in succession to Captain H. T. Baillie-Grohman was signed on the 8th January. (Commander Morse has been given the rank of commodore in the Chinese navy.) Arrangements were made for the training of a further eight Chinese naval officers in England. The officers left China in June to take up their duties.
- 93. In December Admiral Chen, the Chinese Minister of Marine, informed Commodore Morse that he was desirous of reopening the question of warship orders in England and the possibility of an increase in the British Naval Mission. At the time of writing no decision had been reached as to whether it would be worth while to pursue the matter further in view of the desire of the Chinese Government to connect it with a British loan to China.

- 94. In May the Waichiaopu informed His Majesty's Legation that flights carried out by aeroplanes from His Majesty's aircraft-carriers within the harbour of Weihaiwei, or over the land, did not fall within the scope of the agreement attached to the convention for the rendition of Weihaiwei, and that if it was desired to make such flights application must first be made to the Chinese authorities for authorisation in accordance with the revised provisional arrangement governing flights of foreign aircraft over Chinese territory. His Majesty's Legation replied, after consultation with the Commander-in-chief, that they could not admit the contention of the Waichiaopu with regard to flights over the harbour, but were able to assure the Waichiaopu that no flights would be carried out over the land, except in case of emergency, without the previous concurrence of the Chinese authorities. The Waichiaopu made a further attempt to secure that prior to each annual visit of His Majesty's navy to Weihaiwei they should be furnished with an outline of proposed aircraft exercises and be requested to obtain the requisite permission for the flight from the Chinese authorities. After consultation with the Commander-in-chief His Majesty's Legation decided to allow the matter to stand over until next year.
- 95. An International Exhibition of Chinese Art, under the auspices of His Majesty's Government in the United Kingdom and of the Chinese Government was opened at the Royal Academy of Arts in November 1935. The exhibition is intended to illustrate the culture and art of China from early times down to 1800 a.d., and the history treasures comprising it have been chosen jointly by British and Chinese experts from the collection at the Peking Palace and also from private and public collections in Europe and America. The exhibits emanating from China were transported to England in H.M.S. Suffolk.
- 96. The Waichiaopu in a memorandum dated the 27th December, 1934, enquired whether munitions of war unloaded or transhipped at Hong Kong and the re-exported from Hong Kong were regarded as direct exports to abroad. They were informed that the onward passage from Hong Kong to China of munitions, or any other goods, ordered in China from countries beyond Hong Kong was not regarded as a "direct export to abroad," or even as an export or re-export in the sense in which those terms are commonly used in commerce. As regards, however, munitions imported into Hong Kong on consignment, from the United Kingdom or from other countries, no re-exports to China were allowed without the production of a huchao from the Ministry of War at Nanking. In reply the Waichiaopu requested that in all future cases of reshipment to China of munitions imported into Hong Kong or Singapore on consignment, the consignment should not be released on the production of a Central Government huchao until it had been ascertained that the matter was in order. (This procedure is analogous to the securing of an endorsement of the huchao which is required when the shipment is from a country where there is a Chinese Legation.) In reply the Waichiaopu were informed that the suggested procedure would be adopted in the case of Hong Kong, where there is no Chinese diplomatic or consular officer, but that as regards Singapore the huchaos should be endorsed by the Chinese consular officer resident there.
- 97. The question of support to be accorded to representatives of British munition suppliers was referred to the Foreign Office early in the year. This was the result of an allegation by the manager of Messrs. Jardine Engineering Corporation that British firms suffered under a handicap when wishing to import arms into Kwangtung and Kwangsi, as the Italian Government placed no restriction on the issue of export licences and the French Government assisted their firms by making official application for huchaos through the Waichiaopu in a manner which made it difficult for the Nanking authorities to refuse without admitting their inability to control the South-Western Provinces. It was decided by His Majesty's Government that, where reputable British arms exporters were interested, His Majesty's Ambassador could make informal verbal representations in support of applications for huchaos in cases where the failure to obtain a huchao would result in the order being lost by a British to a foreign firm. In no case, however, were the representations to amount to pressure upon the Central Government to grant a huchao for the import of munitions of war which would not otherwise have been authorised by them.

(2) Canada.

- 98. In March the Chinese authorities agreed that the bearers of passports indicating Canadian nationality should be exempted from visa fees.
- 99. On the 28th December, 1934, Mr. C. S. Bissett assumed the duties of Canadian Government Trade Commissioner in Tientsin in succession to Mr. Paul Sykes, who was transferred to Hamburg.

(3) Commonwealth of Australia.

100. In August His Majesty's Government in the Commonwealth of Australia appointed Mr. V. G. Bowden to be Australian Trade Commissioner in China with headquarters at Shanghai. Mr. Arthur L. Nutt was appointed to be assistant Australian Trade Commissioner.

(4) Burma.

- 101. At the end of the year 1934 discussions were proceeding with a view to the establishment of a commission for the delimitation of the southern section of the Burma-Yunnan boundary. An agreement was reached and was embodied in exchanges of notes, dated the 9th April, 1935, between His Majesty's Minister and the Chinese Minister for Foreign Affairs. The first exchange of notes provided that a joint commission should be set up composed of five commissioners, two to be appointed by each side, with a neutral chairman to be nominated by the president of the Council of the League of Nations; the duty of the commission being to define on the ground and fix on the map the undemarcated portion of the line prescribed by the 1897 convention, and to report to the Governments concerned on cases in which local modifications of the treaty line seemed necessary. The second exchange of notes provided that a conference would, if necessary, be convened subsequently at Nanking to negotiate the question of any modifications in the treaty line, and that the results of the report of the commission and of any such subsequent negotiations would be embodied in a new agreement.
- 102. The president of the Council of the League of Nations selected a Swiss officer, Colonel F. Iselin, to be the neutral chairman, and he and the other four commissioners, accompanied by their experts, technical assistants, escorts and commissariat (amounting in all to several hundred men and pack animals) met at Hohsawn, on the Burma side of the frontier, on the 1st December, and at once entered on their enquiry. It is hoped, though without much confidence, that the demarcation of the boundary will be completed within one dry season.

(5) Straits Settlements and Federated Malay States.

103. There is nothing of interest to report.

(6) Hong Kong.

- 104. In June the Waichiaopu returned to the charge in connexion with the evacuation of Chinese residents of Kowloon City to permit of the construction of a public park (see annual report for 1934, paragraph 82). Intimidation by the Hong Kong Government was alleged. In his reply, dated the 5th August, His Majesty's Ambassador denied that there had been intimidation, and pointed out that the residents in question had been offered very generous terms, which they had accepted, and with which they were now expected to comply.
- 105. The question of improving relations between Hong Kong and Canton received consideration during the early part of the year, and it was decided that officials of the Hong Kong Government should pay occasional friendly visits to Canton for the purpose of establishing and maintaining contacts. The chairman of the Kwangtung Provincial Government visited Hong Kong on the 2nd April to say good-bye to Sir William Peel, and he then suggested that a goodwill mission might be sent from the Hong Kong Chamber of Commerce to Canton. The suggestion was followed by a formal invitation, which was accepted, and a mission visited Canton at the end of May and was cordially received.

106. A number of Chinese suspected of complicity in the attempt to assassinate Mr. Wang Ching-wei were arrested in Hong Kong and application for their extradition was made by the Central Government. The proceedings had not been terminated at the end of the year.

(B) Other Countries.

(1) Japan.

107. At the beginning of the year the outlook as regards the relations between China and Japan was brighter than it had been for some time. When the Chinese Government concluded the Tangku Armistice Agreement in May 1933 it was made evident that General Chiang Kai-shek and the National Government had decided that the time had come to face the fact that no effective help was to be expected from the Western Powers, to cut their losses in the north-eastern provinces and to seek to get on terms again with Japan without prejudice to their position on the major issue of Manchuria. There followed a gradual settlement, in the main along the lines desired by the Japanese Kwantung army authorities, of outstanding questions in North China and the neutral zone, culminating early in 1935 in the resumption of direct postal communication between China and Manchuria.

108. There seems little doubt that the policy of seeking a rapprochement with Japan was due to the initiative and decision of General Chiang Kai-shek, although he persisted in playing a rôle of simple soldier and keeping himself in the background, and that he converted his more timid colleagues and the rest of the National Government to his views. Especially important in this respect was the conversion of Mr. Wang Ching-wei, who had hitherto been a strong and vociferous supporter of active resistance to Japan. There ensued a series of conversations and pronouncements from both sides, the upshot of which was in effect a restoration of friendly relations on the basis of setting aside the Manchurian question for the time being, each side undertaking to respect the rights and position of the other as a sovereign State and to do its best to control popular opinion and all unfriendly manifestations.

This situation continued until the end of May when the Kwantung army made another of its sudden and startling moves. The storm broke out of a relatively clear sky, and from the foreign point of view with little or no warning of what was to come. Early in the month two Chinese proprietors of pro-Japanese vernacular newspapers had been assassinated in the Japanese concession at Tientsin. Later in the month there had been an incursion of Chinese bandits from Jehol into the neutral zone. The Japanese military authorities alleged that the local Chinese officials were in collusion with the bandits (a charge strenuously denied by the Chinese side), and that they were responsible for the assassinations, inasmuch as they had not been sufficiently active and sincere in the elimination of anti-Japanese elements and the suppression of subversive activities in North China. They accordingly presented directly to General Ho Ying-chin, as head of the Peiping Branch Military Council, oral demands for the removal of certain Chinese officials, including the chairman of the Provincial Government, and the removal of his troops and those of the Central Government. The Chinese took the necessary steps to meet these improper demands on a voluntary basis, and it was hoped that the matter had been disposed of. A few days later, however, the Japanese military authorities presented General Ho Ying-chin with further demands, namely, that the Hopei Provincial Administration be removed from Tientsin to Paotingfu, that all Kuomintang organs be dissolved or removed from North China, that all anti-Japanese organisations, such as the "Blue Shirts" and the "Volunteers," be suppressed, and that no organisations dissolved or officials dismissed should be re-established or re-employed without Japanese permission, and that no Chinese officials would in future be appointed to North China whose employment might (in the judgment of the Japanese) be detrimental to Sino-Japanese relations. The Chinese authorities again, in the interests of peace, complied with these terms to the best of their ability, but in spite of pressure refused to commit themselves to writing. This, nevertheless, is the "North China Agreement" or "Ho-Umetzu Agreement," to which the Japanese military have since pinned the Chinese down.

- 110. As on similar occasions in the past the Japanese action was marked by threats and demonstrations, including aeroplane flights over Peking, the reinforcement in the form of reliefs of the Japanese garrisons in Tientsin and Peking, and the concentration at Shanhaikwan of an emergency brigade of Japanese troops. Another familiar phenomenon was the distribution in the streets of Peking of anonymous handbills attacking Chiang Kai-shek and Chang Hsuehliang and the Kuomintang, and advocating the restoration of the old Peking Republican Government in co-operation with Japan. The height of the crisis, when the Japanese military were thus menacing the local Chinese authorities with demands and threats and demonstrations of force, coincided with the presentation by Mr. Ariyoshi on the 14th June of his credentials as Japanese Ambassador to the President of the National Government at Nanking, an occasion which was marked by the usual expressions of friendship and goodwill between the two countries.
- 111. A further Sino-Japanese incident occurred in North China early in August when a Chinese colonel commanding the gendarmerie in the Luantung section of the neutral zone and a Japanese soldier were shot by Chinese gunmen at Lanchow station on the Peking-Shanhaikwan Railway. The Japanese military authorities promptly formulated demands, and took the then unusual step of detaining for a fortnight in the Japanese Embassy barracks at Peking the Chinese official who had formerly been Administrative Inspector of the Luantung section of the neutral zone. No explanation of his detention was vouch-safed to the public, and very little comment was allowed to appear in the Chinese press.
- Towards the end of September a message from Japan announced that the Ministries for Foreign Affairs, War and Marine had at last agreed on the policy to be adopted towards China. This "basic" policy was to consist of political and economic co-operation between China, Japan and Manchukuo, with special reference to North China, joint defence against sovietisation, and the complete suppression of all anti-Japanese and anti-Manchukuo activities. The Japanese army's interpretation of this "basic" policy was clearly exposed in a statement handed to the press in Tientsin on the 24th September by General Tada, Commander of the Japanese forces in North China. This statement contained the familiar violent attacks on General Chiang Kai-shek and the Kuomintang. So long as these dominated China there was no hope of the adoption of a friendly policy towards Japan: it was therefore necessary for Japan to disregard them and commence by carving out of North China a paradise where Chinese and Japanese could live together in peace and enlightenment and mutual prosperity, the paradise to be extended by degrees until either General Chiang and his clique changed their attitude sincerely or were squeezed out completely. The basic policy was the subject of a series of conferences covering the last days of September and the first half of October, at which, at Dairen, Shanghai and Tientsin, it was expounded to the Japanese civil and military officials, who would be responsible for its application. The first-fruits of the policy matured only a few days later, when the Japanese consul-general at Tientsin addressed the leading Chinese officials in Tientsin and Peking, charging them with failing to carry out the undertaking referred to in paragraph 109 above, to suppress all anti-Japanese activities and organisations. The Chinese officials replied that they had taken, and would continue to take, energetic measures to that end, and there followed a spate of intense activity on the part of the Chinese authorities, who, under the watchful eyes of the Japanese, rounded up a considerable number of alleged "Blue Shirts." The Japanese gendarmerie also independently arrested a number of Chinese, officials and others, and removed them to their headquarters "for examination.
- 113. The tension was just beginning to relax after these incidents when a fresh crisis was precipitated by the enforcement on the 4th November of the Central Government's new currency control measures, which the Japanese pretended to think were intended as an attack on their interests. In any case, that the Chinese had had the temerity to introduce such measures without consulting them, and, worse still, that Sir Frederick Leith-Ross was, as they wrongly believed, the moving spirit, was sufficient to condemn the measures. The Japanese army were already very worried (or at all events pretended to be) at the possibility of a Communist threat from the north-west, and had some time before approached

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the northern generals with a proposal for the formation of an anti-Communist bloc. The economic threat offered by the introduction of the currency control measures was more than they could stand, and they at once set to work to bring about the administrative and economic severance of North China from the Central Government, which was to their mind the only solution for the maladjustment of Sino-Japanese relations in that area.

114. By means of an army of agents provocateurs incidents were staged at Tientsin and other places in and along the boundary of the demilitarised zone to give the impression of a popular demand for autonomy, while the notorious General Doihara, with the assistance of officers from the Japanese North China Garrison, began that direct wearing down process on the provincial and local officials of Hopei, Shantung and Chahar, to which Chinese officials seem so susceptible. The Japanese demanded that the chairmen of these three provincial Governments and the mayors of the two municipalities of Peking and Tientsin should combine in the establishment of an autonomous bloc embracing the territories under their control, which should be financially and administratively independent of Nanking, and an anti-Communist association, whose declared object should be co-operation with the Japanese forces in preventing the spread of communistic influences in North China. The Chinese officials apparently kept Nanking informed and sought instructions, but the Central Government was as helpless as they were, and could only reply that they should do the best they could in the circumstances. Thus left to their own resources the Northern officials were on the point of yielding to the Japanese importunities when they received on the 19th November instructions from Nanking to break off the negotiations. This decision was connected with events which had been taking place in Nanking, and which are mentioned in paragraph 7 of the present report. Briefly, the National Conference of Kuomintang Delegates, then in session in Nanking, had resolved to present a firmer front to Japanese territorial encroachment, while at the same time using all means to come to a general settlement of outstanding difficulties with Japan on the diplomatic plane. While, therefore, the Northern generals were directed to break off the local negotiations with the Japanese military, diplomatic discussions were initiated at Nanking between the Japanese Ambassador and General Chiang Kai-shek himself.

115. But the Kwantung Army were not to be put off in this manner. Having failed, for the moment, in their major coup, they immediately brought off a minor one. On the 24th November Yin Ju-keng, the Chinese administrator of the demilitarised zone, declared the whole of that zone an autonomous area, and a puppet Government was set up under the style of "The East Hopei Anti-Communist Autonomous Council." The Japanese military forces took the necessary dispositions to prevent any Chinese armed interference with their protégé, and though the Nanking Government instructed the chairman of Hopei to dissolve the rebel organisation and arrest its leader, this was an empty gesture. At the same time General Doihara and his satellites renewed the pressure on the provincial officials to the accompaniment of the familiar aerial demonstrations, threats by "spokesmen" and propaganda, and at length the Central Government, in an attempt to save something—if only the appearance of territorial integrity—from the wreckage, itself set up a Political Council for the two provinces of Hopei and Chahar, with a personnel consisting principally of Northern militarists and ex-Peking Government officials. The council was inaugurated in due course, but its duties and powers were not defined, and, having created it, the Central Government was compelled to leave it to fend for itself, while pinning its own hopes for the future settlement of this tangle on the diplomatic discussions then being initiated in Nanking. Conversations took place between the chairman of the new Hopei-Chahar Political Council and General Doihara, with a view to the abolition of the East Hopei organisation, but without success, since the Japanese army was clearly determined to relax its grip on the autonomous zone only when its own terms for the control of Hopei and Chahar had been satisfied.

116. Since all the functions of government are being slowly paralysed by Japan, and since this is to all seeming part of a deliberate policy to bring China to her knees, the negotiations which are now being initiated in Nanking are of vital importance to China's future. The claims which the Japanese have put forward are far-reaching, if, as is alleged, they comprise the exclusion of all

Western influence, resignation from the League of Nations, an alliance with Japan against communism, the appointment of Japanese military advisers to the Chinese armies, and the creation of an Administration in North China friendly to Japan. Complete acceptance is almost unthinkable, complete rejection in present circumstances almost equally so. Whether there is a middle way the next few months should show.

(2) Union of Soviet Socialist Republics.

- 117 Enquiries of M. Bogolomoff, the Soviet Ambassador to China, revealed that he now considers his headquarters to be at Nanking, not Peking. On the 4th July an address on various aspects of the Soviet Government's policy was given in Nanking by the Soviet Ambassador at the invitation of the Foreign Relations' Committee of the Legislative Yuan.
- 118. Although officials of the Soviet Embassy have strenuously denied that any understanding between the Soviet and China exists, it became increasingly clear during the course of the year that conversations between the two countries have taken place. There is reason to believe that the Chinese Government have been told that the Soviet Government are definitely not prepared to support China unless they are satisfied that China intends to present a united front towards Japanese aggression.
- 119. The question of Sino-Soviet relations is also referred to in the sections on the general internal political situation and Sinkiang.

(3) United States of America.

- 120. The United States Legation in China was raised to the status of an Embassy, Mr. Nelson Trusler Johnson, the United States Minister to China, presenting his credentials to the President of the National Government in his new capacity on the 17th September. Mr. Sao Ke-sze, the Chinese Minister at Washington, presented his credentials as Ambassador to President Roosevelt on the 21st August.
- 121. In reply to an enquiry by this Embassy, the Waichiaopu stated that Chinese interests in Jamaica are still in charge of the United States consul under the arrangement come to between the two countries in 1918.

(4) France.

- 122. Annexes to the Sino-Indo-China Convention of 1930 were signed in the course of the year at Nanking by the French Minister and the Chinese Minister for Foreign Affairs and later ratified (please see tabular statement below). As a result the tariffs on certain goods imported into China from Indo-China were reduced, leading His Majesty's Ambassador to recommend that formal representations should be made to the Chinese Government reaffirming the right of British goods to enjoy similar reductions by virtue of the most-favoured-nation treatment accorded in Annex I of the Tariff Treaty of 1928 and elsewhere.
- 123. Sino-French relations suffered a great loss through the death at Peking on the 23rd September of M. Henry Wilden, the French Minister. Although only 56 years of age, M. Wilden had seen some thirty-five years' service in China and the Far East, and had been French Minister to China since 1929. His funeral was made the occasion for a great display of sympathy, not only by the Diplomatic Corps and the French colony, but also by the Chinese military and civil authorities.

(5) Germany.

124. Following the example of the Japanese and United Kingdom Governments, the German Government decided to raise the status of their Legation in China to that of an Embassy, and Dr. Oskar Trautmann, the German Minister to China, presented his credentials to the President of the National Government as first German Ambassador to China on the 14th September. The German Government have transferred the headquarters of their mission from Peking to Nanking.

(6) Turkey.

125. General Ho Yueh-tsu, the new Chinese Minister to Turkey, presented his credentials in May. In a subsequent statement to the press he anticipated the conclusion of a Sino-Turkish commercial treaty.

(7) Denmark.

126. The Danish Legation was transferred from Peking to Shanghai on the 1st November.

(8) Siam.

- 127. Sino-Siamese relations were embittered by the enforcement of a regulation requiring that in all Chinese schools in Siam a considerable number of hours weekly should be devoted to the teaching of Siamese. The deliberate effect of this was to make it almost impossible for the Chinese pupils to learn their own language. The Chinese residents appealed to the Nanking Government, and there was some talk of imposing an embargo on the import of Siamese rice into China by way of reprisals. This would have injured China as much as it injured Siam and the suggestion was not pressed.
- 128. No progress was made in regard to the long-standing and vexed question of Siam's refusal to accord to China the right of diplomatic or consular representation.

(9) Treaties.

129. Treaties, &c., Negotiated and Entered into Force in 1934-35.

Tabular Statement.

With—	Place and Date of Signature.	Subject.	Place and Date of Exchange or deposit of Ratifications.	Date of Entry into Force.	Remarks.
His Majesty's Government in the United Kingdomand the Govern- ment of India	Nanking, April 9, 1935	Exchange of notes between His Majesty's Government in the United Kingdom and the Government of India and the Chinese Government regarding the establishment of a commission to determine the southern section of the boundary between Burma and Yunnan.			
His Majesty's Government in the United Kingdom	Nanking, Octo- ber 27, 1984	Exchange of notes be- tween His Majesty's Government in the United Kingdom and the Chinese Govern- ment relating to land tenure and taxation in the former British concessions at Han- kow and Kiukiang.			
France	Nanking, May 4, 1935	Annexes to the Sino- French commercial treaty regarding Indo- China of May 16, 1930	Paris, July 20, 1935	July 22, 1935.	

(10) League of Nations.

130. In the course of the year the Chinese Government continued to press for the representation of China on the Council of the League of Nations, which lapsed when China failed to be re-elected to a semi-permanent seat at the session

of the Assembly in September 1934. At a secret session of the 2nd May this year, as a result of a letter from the Chinese representative, the Council decided that the Secretary-General should circulate privately to members a memorandum showing the actual position as regards the election of members to the Council and reviewing the possible methods of giving effect to the Chinese desire. At the time of writing, however, no further progress appears to have been made in the matter.

131. In accordance with the recommendation of the League Council Committee on Technical Co-operation between the League of Nations and China, at its session in September 1934, M. Robert Haas (see paragraph 116 of previous report), Director of the Communications and Transit Section and secretary of the committee, was sent to China in January this year to consult the leading members of the National Economic Council and the authorities responsible for the work of reconstruction in the most important provinces. M. Haas remained in China until May and his report was published by the League of Nations in September. The report was divided into four chapters, the first dealing with the outline and scope of M. Haas's mission, the following two with impressions gathered in Nanking and the provinces, and the last containing general observations and suggestions as to how co-operation could best be maintained between the League and China.

(11) Italo-Ethiopian Dispute.

- 132. His Majesty's Ambassador was instructed to communicate to the Chinese Government the draft reply which His Majesty's Government in the United Kingdom proposed to return to the note of the 11th November addressed to them by the Italian Government protesting against the application of sanctions against Italy by members of the League of Nations, and to urge the Chinese Government to base their reply to the Italian Government on that of His Majesty's Government. Although at first giving the impression that they would meet the wishes of His Majesty's Government, the Chinese Government finally replied to the Italian Government in a somewhat different form in a note which was both brief and friendly, and in which the Chinese action in applying sanctions was attributed entirely to China's obligations under the League, and the hope was expressed that the friendly relations between China and Italy would not be disturbed thereby. On the same date (the 4th December) instructions were issued to the Chinese Customs with regard to the immediate imposition and enforcement of restrictions on commercial intercourse between China and Italy in accordance with the proposals of the Co-ordinating Committee of the League of Nations. In this connexion there arose the question of the advisability of a King's Regulation being issued for the purpose of enforcing the regulations of the Chinese Government on the British subjects in China. It was, however, decided to suspend action in the matter until the Chinese Government enforced the second proposal of the Co-ordinating Committee, they having, up to the time of writing, only enforced the third and fourth proposals.
- 133. Enquiries revealed the fact that neither the American Embassy nor the Dutch, Belgian, French or Spanish Legations had received any instructions with regard to their nationals.
- 134. With regard to Japanese nationals in China, an official of the Japanese consulate-general at Shanghai stated that they would normally comply with any Chinese regulations in force. No Japanese nationals in China were, however, known to be doing business with Italy.

(12) International Settlement, Shanghai.

- 135. Difficulties caused by the Japanese, or arising from their activities, loomed large in Shanghai during the past year. The most serious of these were the following:—
- 136.—(a) A vigorous agitation by the Japanese Residents' Association for greater representation on the municipal council and a share in the administration of the settlement more commensurate with what they conceived to be Japan's position in China. This was coupled with violent attacks on the council accusing

them of extravagance, favouritism and neglect of Japanese interests. In reply to these attacks, which were directed principally against the British as being the leading partners in the administration, the British community took steps to organise the electors of their own nationality in order to make their weight felt at the next municipal elections. At the same time, they examined the position to see in what way legitimate Japanese aspirations could be met without damage to the administration. No definite conclusions had been reached by the end of the year.

137.—(b) The New Life Weekly incident. A small Chinese newspaper printed in the settlement contained an article in which disparaging references were made to monarchs in general, including the Emperor of Japan. The Japanese took the matter up very hotly, both locally and in Nanking. The Chinese and the municipal authorities were as conciliatory as possible, and the editor of the paper was prosecuted in the Chinese court and sentenced to fourteen months' imprisonment.

138.-(c) Early in November a Japanese sailor was shot on an extra-settlement road by an unidentified assailant. The Japanese naval authorities assumed on quite inadequate grounds that the assailant was a Chinese, and the incident and the extreme measures taken by the Japanese to show that they were not to be trifled with roused great feeling between the two nationalities. For some days an exceedingly tense situation existed, but it was tactfully handled and the crisis passed over.

(13) Extra-Settlement Roads.

139. A serious effort was made by the municipal council to effect a settlement of this long-standing question. Agreement was, in fact, reached on what had appeared to be the main obstacle to progress, namely, the claim of the Japanese to a special position in the proposed new police force, but the negotiations came to a standstill on the question of the area which was to be included within the scope of the agreement. The Japanese wished to include some so-called "enclaves" which would undoubtedly have facilitated policing and other administrative matters. The municipal council would also have liked to see the matter settled on these lines, but the Chinese refused to agree, since the absorption of these enclaves into the special area on the confines of the settlement made the whole affair appear too much like settlement extension, and that they are anxious to avoid at any cost.

(14) Chinese Courts.

140. The Chinese authorities for a time pressed hard to get the principle accepted by the council that individual Chinese members of the municipal police could be brought before the Chinese court for acts done in their official capacity on summonses issued at the instance of private prosecutors. The council refused to yield, and was upheld by the Ministers of the interested Powers, and the matter was eventually allowed to drop.

(15) Sino-Japanese Armistice Agreement.

141. The Japanese continued to keep a close watch on the movement of Chinese troops through the demilitarised area, and to insist that advance notice should be given to them in each case.

(16) Pilotage Regulations Revision.

142. It was stated in the annual report for 1934 that proposals satisfactory to the present pilots had been made by the Chinese authorities for taking over the assets, &c., of the Shanghai Licensed Pilots' Association, that our wishes regarding other outstanding points had been met, and that it seemed that the Japanese, who had been consistently opposed to any alteration of the existing system, might be prepared to agree to the regulation as revised, provided arrangements could be made whereby the proportion of foreign pilots should be in accordance with the amount of pilotage fees paid by the shipping of the respective nationalities, and provided Japanese ships used Japanese pilots.

The Shanghai Licensed Pilots' Association, having notified the Inspector-General of Customs that they were prepared to accept the terms offered to them provided the new pilotage regulations themselves were accepted by the Powers concerned, His Majesty's Minister informed the Waichiaopu that he had taken the matter as far as he could, and that he was not prepared to accept the revised regulations until the other foreign Powers had been brought into line. A similar attitude was adopted by the American Legation. The Inspector-General of Customs accordingly concentrated his efforts on obtaining the consent of the Japanese. The latter were, however, adamant in their opposition to any weakening of their rights under the 1868 Regulations, and eventually the Chinese Government reconciled themselves to leaving the Shanghai situation alone for the time being and to enforcing the revised regulations only at those ports and in those districts where none but Chinese pilots were employed. Before this decision was reached difficulties had arisen in connexion with the filling of vacancies in the ranks of the Shanghai pilots. The Chinese Government wished to ignore the 1868 Regulations and to appoint Chinese pilots without reference to the Pilots' Association, but eventually a compromise solution was reached, two of three vacancies being filled by Chinese pilots substantially in accordance with the procedure prescribed by the old regulations, and the third being filled by a foreign candidate.

III.—RAILWAYS.

- 144. There has been no general improvement in the position with regard to Chinese railway indebtedness to British creditors, although the Shanghai–Hangchow Ningpo Railway Loan has been paid off, and payments are now once more being made in respect of the Fengching Loan. The year has been principally remarkable for new construction (for political rather than economic reasons, and largely at the expense of the bondholders in existing lines), and for a number of settlements with Japanese creditors on terms apparently very advantageous to the railways. The Ministry of Railways has remained a profitable political sop to the Canton faction, and a focus for intrigue; in December Chang Kia-ngau, generally supposed to have strong pro-Japanese proclivities, replaced Ku Meng-yu as head of the Ministry.
- 145. There has been in the last months of the year some political interference, the full significance of which it is too early to predict, with the personnel and control of the Peking–Mukden Railway (intra-mural section), some of the earnings of which are reported to have been detained by the "Autonomous Government" set up in the demilitarised zone. The agreement by which 110,000 dollars a month is allocated from the revenues of this line, in contravention of the Peking–Mukden Railway Loan Agreement of 1914 and of the Shanghai–Fengching Railway Mortgage Redemption Loan Agreement of 1914, as security for a loan from Chinese banks to finance the construction of the Lunghai Railway has been renewed, and has been the subject of official protest to the Chinese Government (see annual report 1933, paragraph 208).
- 146. Chinese Government 6 per Cent. Shanghai–Fengching Railway Mortgage Redemption Loan of 1914. Monthly instalments of £5,000 have been set aside, in a special account, from the earnings of the Peking–Mukden Railway, as from August 1935, to accumulate funds for the payment of the annual service of this loan; sums of £6,029 5s. 3d. and £9,022 10s. were remitted to London on the 26th September and the 4th December in respect of the balance of the payment due on the 6th February, 1926, and of the interest and commission due in August 1926. Suggestions made earlier in the year by the Ministry of Railways that the rate of interest should be reduced, which were rejected by the British and Chinese Corporation, have not been renewed. The arrears of interest and bank's commission due on this loan, which amounted in February last to £469,184 5s. 3d., have, therefore, allowing for a further default which occurred in respect of the payment due in August 1935, been reduced by £6,029 5s. 3d., and now amount to £469,178.
- 147. The Shanghai-Hangchow-Ningpo Railway Loan of 1908 was redeemed on the 1st June, 1935, by means of an advance of £225,000 from the British and Chinese Corporation. Twenty per cent. of the daily earnings

continue to be paid into the Special Reserve Account opened in 1932, and are used to pay the monthly instalments of amortisation and interest on the advance referred to above, and also on an advance of 2,500,000 dollars by the China Development Finance Corporation for the construction of the Chien Tang River bridge, both advances being nominally made by a syndicate of the two corporations, and being rendered necessary owing to the impossibility in existing financial circumstances of floating the Shanghai–Hangchow–Ningpo Railway Completion Loan, the agreement for which was signed in 1934.

- 148. The service of the Shanghai–Nanking Railway Loan, 1903, is in default as to three half-yearly instalments of interest and six annual instalments of principal, the total arrears now amounting to £907,062. This line is heavily in debt to the Tientsin–Pukow and the Lunghai Railways, and also to the British Boxer Indemnity Commission. Payment which was made in November 1935 of the half-yearly instalment of interest due in June 1934 was only effected by a loan arranged by the Ministry of Finance with the Bank of China, which is to be repaid by the railway. Ten per cent. of the daily earnings continues to be paid into the Special Reserve Account, and is being utilised to repay the Rolling-Stock Advance.
- 149. No payment has been made in respect of the advances made by the British and Chinese Corporation under the Nanking-Hunan Railway Loan Agreement of 1914. Arrears of interest now amount to over 4,489,598 dollars. With regard to repayment of the advances themselves, it appears that the corporation has been discussing with the Ministry of Railways a project for the construction of a line from Nanking to Nanchang, with extensions, which is based on the 1914 agreement, and recent representations have consequently been confined to demands for payment of interest.
- 150. No payments have been made of interest on the advances made by the British and Chinese Corporation under the Pukow-Sinyang Railway Loan Agreement of 1913, arrears in respect of which amount to over £216,361.
- of the two Tientsin-Pukow Railway Loans, in respect of which no payments have been made, now amount to over £2,587,433. Payments into the Special Deposit Account, which fell into arrears at the end of January 1933, were resumed in August 1935, and monthly payments made since that date have completed instalments due up till the end of April 1934. Coupons No. 34 of the 1908 Loan (German issue), due the 1st April, 1925, and No. 29 of the 1910 Loan (German issue), due the 1st May, 1925, have now been met by payments out of the Special Deposit Account. Investigations appear to show that the net profits of the line as published are actually completely absorbed in meeting debts and "special" expenses of operation. In October the administration of the line, which had since 1932 been governed on the "committee system," was reorganised, and the newly-appointed managing director (who held office, however, only for a few weeks) effected drastic economies in staff and in the purchase of supplies, the results of which it is too early to predict. Meanwhile, in view of the acknowledged obligations of the Chinese Government under articles 8 and 9 of the loan agreements, the defaults in the service of the loans had been brought to the personal notice of the Minister of Finance, who has displayed a lively interest. Since September discussions have been in progress between Sir Frederick Leith-Ross, the Ministers of Finance and Railways, and the Bondholders' Committee in London, with a view to the conclusion of an agreement for a settlement of the loan indebtedness of the Tientsin-Pukow Railway (and of the indebtedness under the Hukuang Railways Loan). The proposals involve cancellation of arrears of interest and reduction of the rate, a customs guarantee and reversion to a large measure of British control.
- 152. The service of the Hukuang Railways Loan is now approximately £3 million in default (British, French, American and German issues). Payment of one half-yearly instalment of interest continues to be paid from the salt revenue.
- 153. Canton-Kowloon Railway.—In September a substantial payment was made from the Special Reserve Account (into which the increased percentage of earnings of the Chinese section are paid—see annual report 1934, paragraph 132)

in reduction of the sterling advance of 1925. No payments have yet been made in respect of the 1907 Loan, the default on which now amounts to over £1,527,847. In August an agreement, perhaps significant in connexion with the eventual construction of the long-desired Canton-Hankow Canton-Kowloon loopline, was made for the issue of through passenger joint traffic tickets between the Chinese and the British sections of the Canton-Kowloon Railway and Canton-Samshui Railway, which is the southern section of the Canton-Hankow Railway (see annual report 1934, paragraph 148).

154. Payments under the agreement for the settlement of the claims of British creditors for materials supplied to the Tientsin-Pukow Railway have been brought up to date and are now being regularly made. The Peking-Hankow Railway have refused to make any similar comprehensive arrangement with British creditors, but have concluded an agreement with the China Import and Export Lumber Company for payment of a capital sum of 28,281·74 dollars in monthly instalments of 1,800 dollars. With regard to Japanese claims against the railways (see paragraph 137 of the annual report 1934), it has now been ascertained that the Peking-Suiyuan Railway did, in fact, conclude agreements on the terms stated both with the Mitsui Bussan Kaisha and with the East Asia Industrial Development Company. This railway also made a similar agreement (which contains, however, special provisions) this year with the Mentoukou Coal Mining Company (a Sino-British partnership) in respect of a loan contracted in 1922. In March 1935 the Mitsui Bussan Kaisha came to a somewhat similar agreement with the Tientsin-Pukow Railway for the settlement of debts for materials supplied between 1916 and 1921; claims amounting to over 6 million dollars and over 2 million United States dollars were scaled down to $4\frac{1}{2}$ million dollars and 4½ million yen, and payment is being made in 300 monthly promissory notes. In April 1935 the Yokohama Specie Bank agreed with the Ministry of Railways to consolidate the 5 per cent. Railway Loan of 1910 (Peking-Hankow Railway), the original amount of which was 10 million yen, on somewhat better terms; repayment is being made by annual payments totalling 19,880,000 yen, beginning May 1935 and ending April 1952, provision being also made for payment of 5 per cent. simple interest. In April 1935 an agreement was made between the Kiukiang-Nanchang Railway and the East Asia Industrial Development Company for the settlement of various loan agreements entered into between 1911 and 1932; the capital sum is agreed at 10 million yen, and overdue interest is scaled down to 8 million yen odd, the former to pay 5 per cent. simple interest, the latter none; monthy payments of 70,000 yen are to be made, to which the railway is to apply a 15 per cent. increase in transportation charges, and the Ministry of Railways is to make up any deficit.

In February a contract was signed by the Ministry of Finance with General Hammond "to proceed to China to examine the Chinese railway system and advise upon its improvement." There remained in the contract as finally signed no trace of the original proposal (see annual report 1934, paragraph 141) for the creation of a railway inspectorate similar to the customs administration. General Hammond and his two assistants reached Shanghai on the 5th May. The Minister of Finance almost immediately requested that His Majesty's Ambassador would mention to General Hammond that the Chinese Government would expect him to formulate some scheme for the settlement of the railway loan obligations. In view of the terms of General Hammond's contract and of the fact that he held no mandate from the bondholders, the Minister of Finance was informed that, as General Hammond and His Majesty's Ambassador understood the position, General Hammond's primary duty was the inspection of the railway system with a view to suggesting reforms leading to greater efficiency of administration; the result of such reforms might be an increase of net revenues, and the settlement of the loan obligations might follow as an indirect result of General Hammond's work. After four months spent in investigations General Hammond submitted his report to the Minister of Finance and, having explained his proposals to General Chiang Kai-shek, left China with his assistants in September, on return to England via Japan, where he discussed his proposals with Sir Frederick Leith-Ross, then on his way to China, one of whose objects was to secure a settlement of China's outstanding obligations under old loans as a prerequisite to any new loan which might result from his visit (see the Financial and Economic section of this report).

- 156. In connexion with Sir Frederick Leith-Ross's negotiations a committee was formed in London in November by the governor of the Bank of England for the protection of the interests of bondholders in Chinese loans. Sir Frederick Leith-Ross received a copy of General Hammond's report from the Minister of Finance, and with the authorisation of the latter General Hammond communicated to the Bondholders' Committee the substance of his recommendations bearing upon the settlement of the loan obligations of the Tientsin-Pukow and Hukuang loans.
- 157. General Hammond's report has not yet been published and only a précis supplied by Sir Frederick Leith-Ross has been seen in this Embassy, of which the following is a brief résumé. In 1934 the railways were 14 million dollars short in redemption of principal and 13,500,000 dollars short in payment of interest. In three or four years, by unification of the operating and financial administration of all the now separate railways, by reduction of staff and fuel consumption, centralisation of workshops and stores, &c., an annual saving of over 13,500,000 dollars could be effected, enabling interest charges to be met but not redemption requirements. In order to attain their best financial results, the railways require new equipment and new lines. At present, of 33 foreign loans, the service of 6 is being met in full, the service of 4 to the average extent of 25 per cent., and that of the remainder not at all. In order to give the railways time and capital to recover and to reorganise, two proposals are made: (a) a loan to China of 30 million dollars having priority to; (b) dollar bonds issued by the Chinese Government (and managed by the Ministry of Finance) in two categories to be exchanged, the first for foreign bonds which received partial payment in 1934 or 1935, the second for foreign bonds which had received nothing in those years, the first to pay no interest for two years, the second to pay for two years the same return made on the original bonds in 1935; after two years both categories to receive the same interest, increasing in the fifth year to a full agreed rate; redemption at a low rate to start in the seventh year. Both Sir Frederick Leith-Ross and the Minister of Finance have expressed doubts as to whether existing bondholders would accept bonds in Chinese dollars. The report does not propose any system of foreign control over the reorganised and unified railway administration, though it is understood that General Hammond made separate suggestions on this head privately to the Minister of Finance, and in general exonerates the existing administrations from charges of corruption and inefficiency.
- 158. Work on the Kwangtung section of the Canton–Hankow Railway is complete, and that on the short uncompleted section immediately to the north is being pushed ahead. It is now reported that the whole line may be finished by June 1936.
- 159. A number of projects, some of which would appear to conflict with existing British and other concessions, are under consideration for the construction of railways in South and South-Western China, including a line from Chungking to Chengtu in connexion with which a Joint Venture Association has been formed under French auspices to cover preliminary expenses, though it is understood that no contract has yet been definitely approved (see annual report, 1934, paragraph 146).
- 160. A seven-year plan for the renovation of the Peking–Hankow Railway, involving expenditure of 22 million dollars, is reported to have been approved by the Ministry of Railways in September. It is understood that the rehabilitation of the railway workshops of this line by the German engineer, von Lochow, which was begun in 1934, is still proceeding.
- 161. Two projects for the extension of the Taoching Railway are under consideration: the first, the extension north-eastwards from Taokow to Tamingfu so long desired by the Pekin Syndicate as an outlet for coal from their mines in Honan; the second, a more ambitious scheme, which includes the above project and also further extensions eastwards from Tamingfu to join the Kiaotsi Railway and westwards from Chinghua either through Shensi to Lanchou or to join the Lunghai Railway at Loyang. The project for the extension to Tamingfu is linked with proposals for a funding scheme for the outstanding indebtedness of the railway (including arrears in default on the Chinese Government Honan

Railway 5 per Cent. Gold Loan of 1905), and with the administration of the line as a branch of the Peking-Hankow Railway.

- 162. The western extension of the Lunghai Railway is now open to traffic as far as Sianfu, and the laying of rails has been completed on a further extension as far as Sienyang in Shensi (see annual report, 1934, paragraph 145).
- 163. Work on the southern portion of the Tatung-Puchow Railway (see paragraph 145 of the annual report, 1934) is reported to be completed, though work on the northern section is believed to have been arrested by tunnelling difficulties.
- 164. The Huainan Railway in Northern Anhwei, which is operated by the Huainan Coal Mines Bureau of the National Reconstruction Commission, is already in operation from the mines south-west of Pengpu to Chaohsien, and the remaining 30 miles thence to Yüchi on the Yangtse opposite Wuhu is rapidly nearing completion (see annual report, 1934, paragraph 147).
- 165. According to a prospectus issued in November 1935 by the Kiangnan Railway Company, the new line in Southern Anhwei is complete from Nanking through Wuhu to Sunchiapu, and plans are only now being made for the construction of the section from Sunchiapu to Kweichi. The company has the concession for the eventual extension of the line southwards to Chaoan on the Kwangtung–Fukien border.
- 166. Arrangements for financing the construction of a line from Kweichi to Yenping in Fukien with funds loaned by Chinese banks are reported to have been made.
- 167. Work is nearing completion in the Yushan-Nanchang section of the Chekiang-Kiangsi Railway, which is expected to be opened in 1936. The German option on the westward extension from Nanchang to Pinghsiang appears to have lapsed, and various schemes for the construction of this section are being considered.

IV.—SHIPPING.

- 168. The Safety of Life at Sea Convention was applied to Hong Kong on the 1st July, 1935, and as from that date certificates issued by the competent Chinese authorities in connexion with that convention, including certificates of competency for officers and engineers, were accepted by the Hong Kong Government as equivalent to those issued by its own authorities (see annual report, 1934, paragraph 169). In September the Hong Kong Government stated that such certificates issued by the Navigation Bureaux at Shanghai, Tientsin and Hankow would be recognised as duly issued by the Ministry of Communications.
- 169. At the same time, the Hong Kong Government stated that it could not accept Chinese passenger certificates as of equal validity with those issued by itself (since it appeared that China had promulgated no rules as to how the number of passengers which a ship is fit to carry should be calculated), and that such certificates could not be regarded as certificates issued in connexion with the convention. These objections having been communicated to the Chinese Government, the Ministry for Foreign Affairs replied in November that provisions governing the number of passengers to be carried were prescribed in regulations under the (Chinese) Merchant Shipping Act, which were revised and promulgated in 1933, and that China's accession to the International Load-line Convention had been communicated to His Majesty's Government in the United Kingdom in August 1935. This information was transmitted to the Hong Kong Government in December and no reply has yet been received.
- 170. In September, the harbour-master at Hong Kong received an application from the Chinese steamship *Ha Yih* for clearance for Saigon with forty passengers from Hong Kong. She was in possession of a safety certificate (and, incidentally, a passenger certificate, which, however, the Hong Kong authorities have not yet agreed to recognise), issued by the Chinese Government. The marine surveyor sent on board at Hong Kong, to measure the vessel with a view to the issue of a Hong Kong passenger certificate, discovered discrepancies between

the ship and her safety certificate, which showed not only incompetency, but downright dishonesty on the party of the Shanghai Navigation Bureau. In the circumstances, the ship was granted only a clearance as a cargo ship. The incident appears to demonstrate the inability of the Chinese Government to overcome the administrative and technical difficulties involved in their accession to the International Convention for the Safety of Life at Sea.

- 171. In March, the Navigation Bureau at Shanghai refused survey certificates to two of the "Dollar" boats, for which the British owners desired inland water passes, explaining that competitors in the Fukien coastal trade had alread complained that too many ships were on that run (see annual report, 1934, paragraph 150). As the result of representations made to the Ministry for Foreign Affairs by His Majesty's Minister, instructions were given by the Ministry of Communications for issue of the certificates.
- 172. The Szechuan Navigation Bureau retains complete independence, though nominally under the Ministry of Communications, and Messrs. Butterfield and Swire have complained that, being presided over by their most formidable trade rival, the bureau is constantly making difficulties. The bureau has, nevertheless, done much to prevent the carriage of unmanifested cargo, which was formerly a serious problem for the shipping companies, and in April 1935 the bureau, with the acquiescence of the companies, instituted a system by which searchers of the Szechuan Provincial Tax Bureau should travel on all ships. The arrangement was not reported to the acting consul-general at Chungking till the 30th May, when, though not entirely approving, and though abstaining from any official cognisance of the matter, he was not prepared to intervene.
- 173. On the 22nd May, 1935, the Special Delegate for Foreign Affairs in Kuangtung and Kuangsi addressed a (circular) letter to His Majesty's consul at Swatow requesting compliance with a claim by the Navigation Bureau at Swatow to control all foreign ships entering and leaving the port (see annual report, 1934, paragraph 154). The letter was ignored, though the matter was discussed in August orally and in general terms with the special delegate at Canton, who was informed that His Majesty's Ambassador took a serious view of the question. No actual interference with foreign shipping appears to have been attempted by the bureau either at Canton or at Swatow.
- 174. A China Navigation Co-operative Society was inaugurated at Shanghai on the 1st May, 1935, by the Government and private Chinese shipping companies, "to administer affairs relative to co-operative navigation in inland waters and along the coast," but nothing has been heard of its activities, if any.
- 175. On the 15th December, 1934, the Pilots' Association accepted, subject to the approval of the Pilotage Regulations by the Powers concerned, the offer made by the officiating Inspector-General of Customs for taking over their equipment and for the dissolution of the association (see annual report, 1934, paragraph 170). After twice postponing the enforcement of the regulations owing to the strong attitude of the Japanese Government, who categorically refused to relinquish the control exercised over Chinese pilotage matters under the regulations of 1868, the Chinese Government in July 1935 dropped the question. Appointments to vacancies, which had continued to be made under the old regulations, though for three months only, were, in July, renewed for twelve months. Meanwhile, the possibility of assuring a continued employment of an adequate proportion of British pilots has been under consideration by the Admiralty, the Foreign Office, this Embassy, and His Majesty's consul-general at Shanghai.
- 176. On the 5th June, 1935, a Yangtze Shipping Pool Agreement was signed, after negotiations which have been carried on intermittently for years, by the Indo-China Steam Navigation Company, the China Navigation Company, the Nisshin Kissen Kaisha, the China Merchants' Steam Navigation Company, the San-Peh Steam Navigation Company (with the Hoong-On Steam Navigation Company), and the Ningpo-Shaohsing Steam Navigation Company. On the 25th June the Nisshin Kissen Kaisha requested a reduction of 15 per cent. in freight rates on their ships on account of the Japanese boycott; this was eventually agreed to and the arrangement, which came into force on the 22nd July, is understood to be working efficiently and to the mutual benefit.

The China Merchants' Steam Navigation Company (see annual report, 1934, paragraphs 157 and 158) has been negotiating not only with British interests, but also with German and Italian, for utilisation of the balance of the loan made from Boxer indemnity funds in 1933 to purchase additional steamers, and secret discussions of a preliminary nature have continued between Messrs. Butterfield and Swire (China Navigation Company) and the Ministry of Communications (represented by T. V. Soong) for some form of co-operation between the two companies. With regard to the utilisation of British Boxer funds for the purchase of new ships, the view of Jardine, Matheson and Co. (Indo-China Steam Navigation Company) is that the China coast and the Yangtze are already over-tonnaged, and that those funds should not be used to foster further competition with British lines. All questions relating to the China Merchants are, however, governed by the deplorable financial position of the company). In January 1935 the Minister of Communications wrote personally to His Majesty's Minister asking him to intervene to dissuade the Hong Kong and Shanghai Bank at Shanghai from pressing for repayment of a loan made in 1912 (against a mortgage of the company's land, wharves and buildings), of which the principal and interest and other charges now amount to over 12 million dollars, and hinting that the bank would be unable to exercise its right to foreclose. After ascertaining the views of the manager of the bank at Shanghai, His Majesty's Minister informed the Ministry of Communications in March that the bank adhered to its decision (conveyed to the Chinese company in December 1934) to proceed to realise its security, without consideration of the nationality of the purchaser, unless some settlement acceptable to the bank were reached. (The bank had in view at the time the possibility of disposing of the property to Japanese, who might be supposed willing to override any objections of the Chinese to the transfer of the property.) No payment or agreement for a settlement has yet been made (although the bank has held up the surrender of its own silver holdings, and consequently those of the other foreign banks, as a lever to force payment—see section on finance). As a result of the financial condition of the company the senior officials resigned in October, and its affairs remain in confusion.

178. Default was made in payment of the instalment of the pensions and other retiring allowances due on the 30th September to British ex-employees in accordance with an agreement made in March 1933. The company admit the liability but state no funds are available. Representations have been made to the Waichiaopu.

179. The operation of the four new ships ordered in 1934 appears to have been successful, especially on the southern routes.

180. No satisfaction has been obtained in connexion with the refusal of the Ministry of Railways to issue to British shipping companies through rail and water bills of lading such as are issued to the China Merchants' Steam Navigation Company. The British companies have requested that our efforts should now be principally directed to the opening of Lienyunkang to their ships (see paragraph 159 of annual report, 1934). Ships trading to this port require a survey certificate issued by the Shanghai Navigation Bureau in order to obtain an inland water certificate, but certificates held by foreign vessels issued by a Lloyd's surveyor, or by the competent authority of the vessel's nationality, are provisionally accepted for the purpose (see paragraph 153, annual report, 1934). Messrs. Butterfield and Swire's ships are surveyed, however, by the British Corporation Register at Hong Kong. In order to obtain recognition by the Navigation Bureau of British Corporation certificates, equally with Lloyd's, the corporation's representative at Shanghai has been appointed Surveyor of Ships at Shanghai. At the same time, in order to enhance their prestige with the Chinese authorities, Lloyd's representatives at Shanghai were given similar appointments, in addition to the already existing consular surveyors, and the Chinese Government have notified the departments concerned that all these persons are authorised to act as marine surveyors at Shanghai of His Majesty's Government, using official seals inscribed "His Britannic Majesty's Government Marine Surveyor, Shanghai." while, the Chinese maintain that the harbour of Lienyunkang is a private property of the Lung-Hai Railway, the sole use of which has been leased to the China Merchants' Steam Navigation Company.

- 181. British shipping companies have experienced a series of incidents with regard to certain sections of their Chinese employees afloat, especially "tea boys" and tally men who are engaged by the compradore staff, pointing to an increase of disorganisation, lawlessness, and insubordination, which has given cause for alarm. This has apparently been due to loss of control by the Seamen's Union (at Shanghai), which was, however, reorganised in September, though with what success is not known.
- 182. Trouble has again been experienced with the activities of the Canton Seamen's Union both at Canton and in Hong Kong. On the 21st March, 1935, an act of gross insubordination was committed at Hong Kong on the British steamship $Tung\ On$ by a greaser, who had been properly prevented by the chief officer from smuggling unmanifested cargo; on arrival at Canton all the firemen left the vessel and refused to return until the owners had transferred the chief officer to a ship which was out of commission. His Majesty's consul-general at Canton made strong personal representations to the chairman of the Provincial Government, who promised to do what he could, but stressed the necessity which the Government was under for dealing tactfully with the union. In May, as the result of a dispute between the Seamen's Union and the Lightermen's Guild, Messrs. Butterfield and Swire's steamship Fatshan was unable to discharge her cargo at Canton. The incident was eventually settled and the ship enabled to discharge future cargoes by compliance with a suggestion made by the Provincial Tangpu, whom the union and the guild had called in as mediators, that Messrs Butterfield and Swire should submit to be blackmailed to the tune of 300 dollars as compensation for a lighterman who had been injured in the fracas (see annual report for 1934, paragraphs 160–3).
- 183. An order from the Shanghai Special District Court in December for the seizure of a British-owned sailing yacht appears to have been made under a misapprehension, due to misrepresentations by the native police officer concerned, who wished to satisfy a private claim against the Chinese servant on board. His Majesty's consul-general made representations to the mayor, requesting the punishment of the police officer.
- 184. With the concurrence of the Hong Kong Government and the approval of the Foreign Office, British protection in China was withdrawn in May from the registered British steamship Winglee, under the powers conferred by the China Ports Amendment Regulations No. 1 of 1928; the ship, though she remains entitled to fly the red ensign, will be unable to trade in China waters, being unqualified by her ownership to register under the port regulations and hence unable to obtain port entrance.
- 185. The question of the carriage of Chinese troops in British ships which scarcely arose in 1934 (see annual report, 1934, paragraph 167) has given rise to much correspondence in 1935. In January the Ministry for Foreign Affairs informed His Majesty's Minister that the Ministry of War desired to charter foreign steamers on the Upper River for transportation of Chinese troops to Szechuan in connexion with the anti-Communist campaign. British companies were informed that they must decide for themselves; they replied that they were willing to do so in an emergency on condition the troops were unarmed, adequate payment was made, and a British naval guard provided. The Commander-inchief stated that the Rear-Admiral, Yangtze, would furnish provisional guards. Early in March the two British shipping companies intimated that, as the state of emergency had passed, they were no longer prepared to carry troops, but at the end of March local negotiations were resumed between the companies and the Chinese authorities, and the suggestion was made by Butterfield and Swire that, Chiang Kai-shek having asked for a list of foreign firms' grievances, the carriage of troops might be accompanied by suppression of the Wanhsien boycott. The British companies appeared to have received no applications from the Chinese authorities to carry troops.
- 186. In June the acting consul-general at Chungking complied with a request from Mme. Chiang Kai-shek for a brief history of the Wanhsien boycott, suggesting that, without going back into the rights and wrongs of the incident, Chiang Kai-shek might now give instructions for the boycott to cease; his decision to do so, provided there was no publicity, was communicated to the British

shipping companies, who were able to commence shipping cargoes at Wanhsien before the end of June, after a lapse of nine years.

- 187. In September His Majesty's consul-general at Canton reported that small parties of Chinese troops, who had refused to give up their arms, had been travelling locally inter-port on ships under the British flag. Representations had been made to the military headquarters, Canton, who had issued instructions that this must cease, but had expressed the hope that no objection would be made to small parties provided they deposited their arms with the captain of the ship. In deference to the views of the Commander-in-chief, the number in such parties was limited to twelve, without, however, laying down hard and fast rules.
- 188. In this connexion the Foreign Office in March set forth the following considerations as governing the attitude to be adopted: The question of the carriage of Chinese troops is one of expediency; a request should only be passed to British companies after it has been made formally by the Ministry for Foreign Affairs; the Embassy should act only as a channel of communication and avoid any question of responsibility.
- 189. In December His Majesty's consul at Ichang, at the request of the American local Co-Assistant Auditor of Salt Revenue, and with the concurrence of the British shipping companies, arranged that salt revenue officers should search the companies' ships provided they were unarmed, carried a certificate of authority countersigned by His Majesty's consul, and gave a receipt for manifested cargo seized.

V.—MINING.

- The lively interest displayed by Japanese in the affairs of the Kailan Mining Administration is referred to in the trade section of this report. In view of enquiries known to have been made by the Japanese consul-general, the British and the Chinese co-general manager of the Administration arranged in March that he should be supplied with a copy of the supplementary agreement signed in August 1934 (see annual report 1934, paragraph 176), and with the documents referred to in the schedule, a copy of which had in any case already been supplied to the Provincial Government. As the result of continued Japanese activities in the Shihmenchai coal-field in the vicinity of the Administration's mines and its port at Chinwangtao, it was decided in June, in order to make clear that the British interests in the Administration's property had not been overlooked, to station a British man-of-war at Chinwangtao and/or Peitaiho. Since July there has been constant unrest in the mines area, secretly fomented by local Japanese, both of the ronin and of the petty military official type, though the actions of the senior Japanese officers have been singularly helpful and correct. The trouble culminated in the removal, ostensibly by the Chinese authorities, in September of the chief of police in the Mines Area, who had been nominated by the Administration and had proved entirely satisfactory, and his replacement by a creature of the more undesirable Japanese element. In September, also, the Administration was obliged publicly to deny reports in the Japanese press that they had proposed a sale of their interests to Japanese. connexion with the trouble which had arisen with the mines police, one of the language officers attached to the military attache's office visited the mines in November. On his return he reported that, though there appeared to be certain secret pro-Japanese organisations operating in the mines area which were a potential source of trouble, the situation was as satisfactory as could be expected, and the attitude of the local Japanese military officials on the whole most reasonable.
- 191. Meanwhile, apprehension of Japanese designs on the Administration's property was an incentive to the Chinese partners to propose, and to the Nanking authorities to consent to, the deletion from the 1934 agreement of clause 22, which gave the Chinese Government the right to demand registration of the Administration as a Chinese company. The rescission of this clause was approved by a rescript of the Ministry of Industries dated the 24th July, 1935.
- 192. As the result of negotiations commenced in April, involving a payment to the then about to retire Minister of Industries of 134,000 dollars for the lease of a small area claimed by the Government within the Administration's

concession, the Ministry of Industries, on the 29th November, issued a regular mining permit for the whole area claimed by the Administration, without raising any question, either of the registration under Chinese company law of the Chinese Engineering and Mining Company, or of the reconstitution as a Chinese company of the Administration. An official communication was sent on the 12th December by the Ministry for Foreign Affairs to this Embassy stating that the permit had been issued, and certified copies of the documents were received from the Chinese Engineering and Mining Company and filed in this Embassy on the 30th December.

193. Interference by the East Hopei Autonomous Government with the operations in the Mines Area of the representatives of the Consolidated Tax Bureau led to the despatch from this Embassy on the 19th December of a probationer vice-consul on a brief visit to the mines to act as an observer, it being hoped that his presence there might deter the representatives of the Autonomous Government from violent and precipitate action, such as preventing the Administration's coal from leaving the mines. Up till the end of the year there had been no interference with the Administration's operations. They have in stock at Chinwangtao 800,000 tons, covered by proper tax certificates issued by the Consolidated Tax Bureau, which the customs are consequently able to pass for shipment. Fresh coal leaving the mines is covered by similar tax certificates, issued, however, and surcharged by the representatives of the Autonomous Government. Meanwhile, the Administration does not desire to pass this fresh coal through the customs. Payment of the Consolidated Tax in respect of these certificates issued at the mines is normally made monthly to the Consolidated Tax Bureau at Tientsin. Pending clarification of the situation, payments are now being held in suspense.

194. No trouble has occurred or threatened in the course of 1935 at the Peking Syndicate's mines. At the request of the syndicate His Majesty's Ambassador on the 15th November made formal representations to the Ministry for Foreign Affairs regarding the non-production by the Honan Provincial Government of confirmation of amounts of principal and interest outstanding on a loan of 300,000 dollars made by the syndicate in 1925, required by them for their London auditors. Minor difficulties have been experienced in connexion with transport on the Taoching Railway of coal produced by the native pits. These appear, however, to have been met, partly by apparently arbitrary orders issued by Chiang Kai-shek, and partly by agreement between the Chungfu Mining Administration and those native pits which hold mining permits. The syndicate have under consideration a scheme for the purchase of their interests in Honan by the Chinese Government. There have been indications (somewhat vague) that Japanese may be contemplating the possibility of acquiring an interest in mines in that area.

195. The affairs of the Mentoukuo Coal Mining Company (see annual report 1934, paragraph 172) have given rise to no anxiety, and no correspondence with this Embassy, during 1935. No further pressure has been brought to bear for registration of this Sino-British partnership as a Chinese concern.

196. The Chinese coal-mining industry has gone from bad to worse, chiefly owing to ineffective control of an almost infinite number of small "illegal" native pits, and to the uneconomic and unprincipled manner in which the larger native concerns are financed and operated. Cut-throat competition has ensued, with the result that all the native concerns are on the verge of bankruptcy, and the foreign-controlled mines are making little or no profit. Various measures have been suggested and put in force for control of unlicensed pits, for reduction of railways freights, and for readjustment of the mining taxes. On the 1st August, 1935, an agreement was made between the Ministry of Industries and Messrs. George McBain (who are the British partners in the Mentoukuo Coal Mining Company), for a loan by the latter to the former of 10 million dollars for the relief of the mining industry. This sum has been placed at the disposal, for appropriation to various coal mines, of a Mining Finance Readjustment Committee (of which C. T. Wang, the managing director of the Liuhokou Coal Mining Company, is chairman), the general duties of which are understood to be to give financial assistance to the coal industry, and to effect a reduction of taxation and transportation charges. In connexion with this agreement the

Japanese consul-general at Nanking made with the Ministry for Foreign Affairs a reservation of the rights of Japanese in connexion with certain coal mines in Shantung. The terms of this agreement have not been published, but a copy has been communicated by Messrs. George McBain to this Embassy.

197. Mention of the affairs of the Hunan Antimony Syndicate, and of the sales monopoly of South Kiangsi wolfram, held by the military authorities in Kwangtung, is made in the trade section of this report. The new Hwainan Railway, the Tatung-Puchow Railway, and the westward extension of the Chekiang-Kiangsi Railway will open up new outlets for the coal mines in Northern Anhwei, Shansi and Kiangsi respectively. In this connexion, see also the paragraphs relating to Japanese economic penetration, with reference to the projected railways from Taku to Shihchiachwang and from Tsinan to Tamingfu. No particulars are available, but it is reported that the Japanese are about to exploit more effectively the iron mines near Lungkow in Shantung in which they have interests. The tin mines in Yunnan are reported to be making large profits, in spite of the lawless conditions which prevail in the mining area.

VI.—FINANCE.

- 198. The Government has continued in desperate and ever more urgent need of funds, owing largely to the undiminished demands of the military, whose actual expenditure has been cloaked by manipulation of the customs returns of arms and ammunition imported. Apart from any question of general currency reform or economic reconstruction, efforts to obtain a foreign loan of some kind on any terms have been continually made, T. V. Soong having been specially selected for this purpose by Chiang Kai-shek and the Minister of Finance (particulars are contained in subsequent paragraphs).
- 199. The budget for the 24th fiscal year, 1st July, 1935–30th June, 1936, showed revenue 957,154,006 dollars (including 109,793,197 dollars, the proceeds of loans for ad hoc purposes entered on the debit side also, and 70 million dollars for new borrowing and allowing 64 million dollars for cost of revenue services). or net revenue 713,360,809 dollars, and expenditure of 957,154,006 dollars, of which 321 million dollars is for military purposes. Estimated increases of revenue over last year are in respect of new sources, while insufficient allowance appears to have been made for probable decreases in the revenues from the principal revenue-paying departments. The estimates were for the first time published at, instead of long after, the end of the previous financial year: this has been hailed as a sign that the Government's efforts at budget reform are meeting with success.
- 200. In pursuance of resolutions adopted at the National Finance Conference in 1934, instructions were issued for the enforcement of a district budgetary system in accordance with which the Provincial Governments approve and submit to the Ministry of Finance the budgets of the local governments under their jurisdiction. On the 8th September, 1935, the National Government issued further regulations for the control of local budgets providing: for publication of the budgets as approved; for punishment of local officials collecting taxes not authorised in the budgets or appropriating revenues to purposes other than those specified; for complaints by the public against irregularities; and for adherence to the approved budgets as published without amendment.
- 201. A very confidential statement communicated by the customs shows that the total amount released to the National Treasury in 1934 was 50,315,579 dollars, including over 14 million dollars from the 5 per cent. revenue surtax and 4·2 million dollars allocated for Peking and Tientsin educational expenses. (See annual report 1934, paragraph 179.) This surtax has been continued till the 30th June, 1936. The corresponding figures for 1935 were 46,909,000 dollars released, including 13,509,000 dollars from the 5 per cent. revenue surtax and 4,200,000 dollars allocated for Peking and Tientsin educational expenses.
- 202. With regard to existing indebtedness, loans secured on the customs (with the exception of the Tientsin-Pukow and the Hukuang Railways Loans) have again been punctually met, while the other obligations of the Government, including railway loans, still remain heavily in default.

203. In addition to the settlement of certain Japanese claims in respect of railway loans (see section on railways), agreements were concluded with other Japanese creditors: (a) On the 1st November, 1934, between the Ministry of Communications and the East Asia Industrial Company for telegraph loans; (b) on the 1st January, 1935, between the Ministry of Communications and the China Japan Industrial Company for telephone loans; and (c) on the 29th December, 1934, between the Shantung Provincial Government and the China Japan Industrial Company for a loan contracted for provincial development in 1925. The terms on which these settlements have been made are not more favourable than those offered, and in some cases accepted, by British creditors whose prospects of effecting settlements of their claims do not appear to have been prejudiced.

204. Certain British creditors of the Ministry of Communications have also agreed to settlements (see under claims section), and a settlement of indebtedness under an old loan for railway material has also been agreed (see under railways section), but no progress has yet been made in connexion with the Vickers and Marconi Loans, or the Hankow Improvement Loan and the Anhui Provincial Government Loan, and other outstanding British loan obligations. A committee of British bondholders in Chinese loans has been formed in London (see railways section).

205. In April 1935 operations under the Cotton-Wheat Loan (see annual report 1934, paragraph 181) were terminated after only eighteen months in which transactions had been fairly satisfactory.

206. On the 1st April the Ministry of Finance issued at par a 6 per cent. 100 million dollars 24th Year (1935) Currency Loan, redeemable in ten years, "to strengthen the capital of the bank, refund loan advances, stabilise the currency situation, and facilitate relief of industry and commerce." The loan was secured on "the newly-increased customs revenue," and a protest was made against this in representations relating to defaults in the service both of the Tientsin-Pukow Railway Loans and of the Hukuang Railways Loan. This bond issue was part of a policy for strengthening the Government's interest in the Bank of China, and the Bank of Communications, by increasing the Government's share in their capital, and for increasing the capital (entirely Government owned) of the Central Bank. It was followed by a reshuffling of the more important posts in the Central Bank and the Bank of China, as a result of which Li Ming and Chang Kia-ngau, the chairman and the general manager (both anti-Soong and reputedly pro-Japanese) were replaced by T. V. Soong and Sung Han-chang, while Chang Kia-ngau was offered the uninfluential position of co-deputy governor of the Central Bank. Government representation on the boards of directors and of supervisors was greatly increased. These measures were followed by a statement that it was intended to make the Central Bank a bankers' bank, the Bank of China a foreign trade bank (avoiding competition with the Central Bank as far as Government business was concerned), and the Bank of Communications an industrial bank.

207. The Central Trust of China, affiliated with the Central Bank of China, was inaugurated at Shanghai on the 1st October, 1935, to handle the savings of business employees and servicemen, the purchase of supplies for and to underwrite the insurance on Government and business institutions, the issue of premium bonds, and trust business generally. The boards of directors and of supervisors include most prominent bankers. Dr. Kung is chairman of the board of directors. Chang Kia-ngau was appointed general manager, but later, when appointed Minister of Railways in December, was succeeded by Churtong Yih.

208. Developments in connexion with the institution of a "mortgage bank" are described in subsequent paragraphs.

209. On the 29th June, 1935, was issued at 98 a 6 per cent. 23rd Year (1934) 100 million dollars Customs Revenue Loan, redeemable in ten years, for the purpose of making up the deficit in the national budget for the 23rd fiscal year (1st July, 1934–30th June, 1935), the Ministry of Finance being authorised to retire and destroy 23rd Year (1934) Customs Treasury Notes (see annual report 1934, paragraph 182) to the amount of 50 million dollars, and release the sinking fund in connexion with them for this new issue. The effect of the new issue is to convert 50 million dollars of the 1934 treasury notes, which were redeemable in

six years, into a longer term loan redeemable in ten years. The issue of this loan, which is secured on the customs, formed the subject of protest in connexion with defaults in the service of the Tientsin–Pukow Railway Loans and of the Hukuang Railways Loan.

- 210. The Ten Million Dollar Telegraph 6 per cent. Loan of the 24th Year (1935) was issued on the 1st October, 1935, at 98, repayable in seven and a half years, and secured on the surplus income of the international telegraph services of the Ministry of Communications. The whole issue has been deposited with a Chinese banking syndicate as security for a cash loan of 6 million dollars at 8 per cent., which is to be repaid by the redemption of bonds to that value, an additional 2 per cent. being meanwhile paid on them. The remaining 4 million dollars will then be released by the syndicate. The object of the issue is to readjust and expand the telegraph, telephone, and radio services. Three million dollars of the cash loan raised on the bonds has been used to repay advances from other banks previously borrowed by the Ministry for the purchase of materials.
- 211. On the 1st November, 1935, the 24th Year (1935) Flood Relief Loan for 20 million dollars was issued at 98 in 6 per cent. bearer bonds repayable in twelve years, amortisation by drawings to commence in the sixth year. Interest will be paid from the National Treasury's Flood Relief Reserve Fund: funds for repayment of the principal are to be drawn from "the newly-increased customs revenues." In view of the eleemosynary object of the loan no protest has been made against this hypothecation of customs revenues. It is proposed that public functionaries receiving salaries of 101 dollars a month or more shall be paid 10 per cent. of their salaries in bonds of this issue for a period of two months as from January 1935.
- 212. As supplementary to the statement of the financial situation contained in paragraphs 185–188 of the annual report for 1934, it should be noted that the disappearance of silver entailed an immediate contraction in the basis of credit and a corresponding deflation of prices, the effect of which was specially serious to Shanghai, where there had been a large speculation in real estate in which both the public and the banks were involved. The collapse of real estate prices which ensued gravely compromised the banking system, which in turn affected the possibilities of Government financing, as the Government are largely dependent on borrowing from the banks to meet the budget deficit. In spite of the imposition in October 1934 of the export tax and equalisation charge on silver exports exchange was still over-valued: smuggling of silver out of the country continued unabated; the balance of payments continued adverse; and the Government had still to find means of financing its expenditure. The dollar was subject to heavy speculative attacks and the country was faced with a financial crisis which threatened to degenerate into a panic.
- At the end of November 1934 the Chinese, as a temporary measure to restore confidence, put forward a proposal that the Hong Kong and Shanghai Bank and the Chartered Bank of India, Australia and China should, against the deposit of silver in Shanghai, grant a credit in London of £10 million, which would enable the Stabilisation Committee to sell sterling freely, in order to maintain and gradually raise the rates fixed with a view eventually to the removal of the export duties and the restoration of the free movement of silver when the rate had reached parity with silver abroad. This scheme fell through because the project was not viewed favourably in London and the Chinese would not agree to the transfer of the necessary silver from the Chinese banks to the custody of the foreign banks concerned. An alternative similar scheme, by which the silver required as security for the sterling credit should be loaned from Hong Kong by the Hong Kong and Shanghai Bank and shipped to Shanghai, also fell through, because the security offered for the loan was unsatisfactory. At the end of December 1934, T. V. Soong, to whom the conduct of negotiations for a loan had been entrusted, proposed, and the Hong Kong and Shanghai Bank in Shanghai advocated, yet another scheme; a loan of £20 million to be made to the Chinese Government by the consortium, of which half would be brought to China for reduction of internal debt, thus releasing customs funds as security for the loan, the other half being utilised to pay instalments of Chinese Government obligations due abroad, thus eliminating demands for foreign currencies and keeping exchange steady. Retirement of 100 million dollars 23rd year treasury notes would release an annual

customs charge of 16,800,000 dollars, which, plus customs surplus of 28 million dollars plus revenue surtax of 13 million dollars, were offered as security for the loan of £20 million, repayable in five years. Meanwhile, the Central Bank would assist those native banks whose position was precarious, until news of the loan should, by restoring confidence, render such assistance unnecessary.

- 214. All these proposals, while they might temporarily have restored confidence, would have done nothing to correct the adverse balance of payments or to mitigate the effects of a high exchange continually tending to rise on account of America's silver-buying policy. In these circumstances His Majesty's Government in the United Kingdom were not prepared to relax the ban on foreign lending. The Chinese authorities and the Hong Kong and Shanghai Bank were informed in January that any proposed loan or credit must form part of some comprehensive scheme of monetary reform which would include the divorce of the Chinese dollar from silver and its linking with sterling, the fixing of a rate of exchange which would assist exports and correct the balance of payments, and the balancing of the budget, and, moreover, that full co-operation by the other consortium Powers, including Japan, was essential.
- 215. The year opened with the financial situation at the gloomiest, with rumours of devaluation, of a probable declaration of a moratorium by the Chinese banks on their note issues (which had rapidly expanded while public confidence in the existence of adequate reserves diminished), of manipulations of the silver equalisation duty by T. L. Soong, Mme. H. H. Kung and their family clique, and of a breach between them and other Shanghai bankers headed by Li Ming and Chang Kia-ngau.
- 216. In February, a Monetary Advisory Committee of the Ministry of Finance was set up with Chang Kia-ngau (who had been opposed to the loan proposals of T. V. Soong and the Hong Kong and Shanghai Bank) as its principal member. As a result of its recommendations exemption from payment of the export duty and equalisation charge imposed on the 15th October, 1934, was granted on re-export to imports of silver as from the 19th February, the object being partially to restore the free silver market and to encourage the inflow of the metal.
- 217. Towards the end of February a financial crash seemed imminent, and the Hong Kong and Shanghai Bank and T. V. Soong urged reconsideration of the £20 million loan proposal. His Majesty's Government maintained their previous attitude and suggested full discussion with the Governments of Japan and the United States with a view to co-operation with China in considering remedies for the situation, adding that cordial relations between China and Japan were the only basis for that general détente in the Far East without which there could be no satisfactory solution of any of the problems with which China, Japan, Great Britain and the United States are faced. At the same time, the general attitude of His Majesty's Government was explained to the Governments of the United States and of Japan: the former expressed interest and general agreement, but offered no concrete suggestions; the latter expressed warm appreciation and willingness to co-operate in considering the best means of helping China. The Chinese Government concurred that the only basis for peace in the Far East was co-operation between all the Powers concerned, but made it clear that they disliked the idea of Japanese participation in any loan.
- 218. On the 6th March a communiqué on Sino-Japanese relations was issued by the Vice-Minister for Foreign Affairs at Tokyo containing the statement that "Japan will flatly refuse to participate in a discussion to give international economic assistance to China." In conversations which His Majesty's Minister held at about this time with the Japanese Minister, and the Japanese consulgeneral at Shanghai, both appeared to deprecate any loan for currency reform purposes, though the latter stated he had informed T. V. Soong that Japan would be ready to examine with the other Powers what it might be possible to do.
- 219. On the 15th March, T. V. Soong, while emphasising the opposition anticipated from Japan, told His Majesty's Minister that China would accept the principle of joint action; he added that he, the Minister of Finance, and Chiang Kai-shek had, in view of the failure of the loan proposals and the continuance of America's silver-buying policy, come to the conclusion that China must

abandon silver and stabilise the dollar at a low rate by linking it to some foreign currency, a process to be facilitated by sale of her silver to America, but that a large foreign loan and credit would be required.

- 220. The Chinese official reply on the 18th March contained no concrete suggestions and sought the views of His Majesty's Government as to how to facilitate preliminary discussions. They were advised to communicate this reply and make a similar request to the other interested Powers.
- 221. In view of the technical difficulties involved His Majesty's Government at the end of March decided to attach a financial expert to His Majesty's Legation. This decision was communicated to the Chinese Government, and also to the American, Japanese and French representatives in London, with the hope that their Governments would make similar appointments. It became clear, however, in discussions which His Majesty's Minister had with his American and Japanese colleagues that their Governments had been informed that His Majesty's Government proposed a conference of experts at Shanghai and that the proposal was deprecated.
- 222. In the ensuing weeks it became increasingly obvious that the Chinese were obsessed with the idea of Japanese opposition and still desired, if possible, to implicate His Majesty's Government in individual negotiations, and on the 16th April His Majesty's Minister informed the Minister of Finance that any draft proposals received from the Chinese Government would be communicated to the other Governments concerned.
- 223. In mid-April a further rise in the price of silver, due to American buying, created renewed nervousness, and T. V. Soong obtained from the foreign bankers (including the Japanese) on the 14th April an informal assurance that they would abstain from exporting silver. On the 17th April, His Majesty's Minister was informed by M. Monnet, on behalf of T. V. Soong and the Minister of Finance, that they wished to suggest a conference of international financial representatives at Shanghai, who might formulate concrete proposals for radical currency and economic reform, but that meanwhile they urgently desired, as a necessary preliminary to and integral part of such eventual reform, the immediate issue of a sterling loan in Shanghai by foreign local interests to restore confidence and to expand credit by the purchase of Government bonds held as security of the Chinese banks.
- 224. In view of the American and Japanese reaction to the proposal to appoint financial experts, and of the fact that none of the Governments concerned had made any direct response to the proposal, M. Monnet was informed on the 26th April that a suggestion for a financial conference appeared to be unwise at the moment; and that with regard to the desired loan it seemed better to await the arrival of the financial advisers. The Chinese urged the speedy appointments of the advisers, for which they would wait. Early in May M. Monnet stated that the Japanese consul-general had told him Japan would participate in a joint loan if satisfied it were non-political, for the benefit of China as a whole, and to be used for specified purposes; a few weeks later M. Monnet communicated a similar message, said to have been given to T. V. Soong by a Japanese banker who had consulted political leaders in Japan.
- 225. At the end of May it appeared that the Minister of Finance, unknown to T. V. Soong, was flirting with the idea of abandoning the proposals for an international loan in favour of a gold loan from the British banks in Shanghai.
- 226. Meanwhile, the financial situation was aggravated by a recrudescence of the clandestine export of silver, much of which passed through Hong Kong, and on the 6th June the colony, as the result of representations from the Chinese Government, prohibited the export to any country other than China (except under licence) of any silver coin minted in China and any silver bullion other than silver bars, the product of refineries outside Hong Kong and China.
- 227. The ever-deepening depression, accompanied by native banks' failures, led to a crisis, in which financial collapse was only averted by advances from the Government banks to the Shanghai Native Banks Guild of bonds to the value of 25 million dollars to be loaned to member banks able to put up adequate collateral.

- 228. On the 8th June the Minister of Finance and T. V. Soong were informed that His Majesty's Government, desiring that the most authoritative advice at their command should be made available through His Majesty's Minister to the Chinese Government in co-operation with the other Governments concerned, had appointed Sir Frederick Leith-Ross, the Chief Economic Adviser to His Majesty's Government and vice-chairman of the Economic Committee of the League of Nations, to leave England early in August as temporary financial adviser to this Embassy. A similar communication was made to the French, Italian, Japanese and American representatives in China. (On the 1st August Mr. E. L. Hall Patch was appointed to accompany Sir Frederick Leith-Ross on his mission to China, and, at the conclusion of the mission, to act as financial adviser to His Majesty's Ambassador.)
- 229. On the 12th June M. Monnet informed His Majesty's Ambassador that he was considering the constitution of a mortgage bank to advance money to banks against their frozen real estate assets, and that such a scheme would entail a lifting of the Treasury ban on foreign lending to enable the issue of local sterling loan by the British banks.
- 230. On the 25th June M. Monnet, without reference to the mortgage bank scheme, and purporting to speak after concurrence with but not on behalf of T. V. Soong, the Minister of Finance, and the Hong Kong and Shanghai Bank, urged that, in order to hold the situation until the arrival of the financial experts, the financial position demanded the immediate issue of a sterling loan of between £5 million and £10 million to the Government banks to enable them to grant short-term loans to deserving industries and for supporting solvent banks whose assets were temporarily frozen; such a loan, secured on customs surplus or customs 5 per cent. revenue surtax, could take the form either of an issue in Shanghai underwritten by local foreign and Chinese interests or of a credit granted by the Bank of England to the Central Bank of China; if a large scheme resulted from consultation with the financial experts, this loan would be exchanged for bonds in the larger issue; if not, His Majesty's Treasury would be asked to obtain a quotation on the London Stock Exchange for the present issue.
- 231. At the end of June the Japanese banker, who had stated earlier in the month that on certain conditions Japan would participate in a loan, stated to the manager at Shanghai of the Hong Kong and Shanghai Bank that Japan would certainly not give China financial assistance until she mended her anti-Japanese ways, that it was unlikely Japan would appoint an expert, that he saw no reason why the Japanese banks should continue to observe the informal agreement not to export silver, and that the Japanese military thought it might be as well to let China lapse into financial chaos and that they contemplated turning out the present Chinese Government. His Majesty's Ambassador at Tokyo was of opinion that these views did in fact represent the attitude of the Japanese military, and that it was useless to expect anything but opposition from Japan to any scheme for international financial assistance to China, though a possible alternative might be joint British-Japanese assistance.
- 232. Throughout July the financial and political situation became graver; there were increasing indications of Japanese support for a separatist movement in the north accompanied by connivance at wholesale clandestine exports of silver to Japan and Korea, and of Japanese pressure at Nanking to force the Chinese to commit themselves politically and economically to Japan before Sir Frederick Leith-Ross's arrival; financially, the position went from bad to worse, owing largely to a growing lack of confidence, and there were widespread rumours of impending devaluation and a moratorium for the Chinese banks.
- 233. So serious did the situation appear to be that, at T. V. Soong's request, His Majesty's Ambassador went to Nanking on the 10th July to discuss matters. T. V. Soong urged, and the Hong Kong and Shanghai Bank advocated, the palliative loan proposal put forward by M. Monnet on the 25th June; the scheme would be made to appear in the form of a proposal by the Hong Kong and Shanghai Bank, who would invite other banks (including the Japanese) to associate themselves in the undertaking. After reference to the Foreign Office, the Minister of Finance, T. V. Soong, and the Hong Kong and Shanghai Bank were informed on the 26th July that His Majesty's Government could agree to

nothing which might prejudge the position before Sir Frederick Leith-Ross's arrival and that the reasons for not relaxing the ban on foreign lending still held good. The Minister of Finance and T. V. Soong expressed grave apprehensions as to the financial and political outlook, and the latter animadverted bitterly on the failure to obtain this "paltry loan," which would have enabled him to hold out against the Japanese and those Chinese (including Chiang Kai-shek) who were dubious of any financial assistance from England, adding that a high official in Japan had recently definitely offered a loan to stabilise Chinese currency.

- 234. The head manager of the Hong Kong and Shanghai Bank at Hong Kong urged that the palliative loan proposed was preferable to financial collapse or Japanese dominance, which otherwise seemed inevitable, and His Majesty's Ambassador in reporting to the Foreign Office endorsed this view, adding that any tangible proof of His Majesty's Government's desire to assist would have a political value.
- 235. The manager at Shanghai of the Hong Kong and Shanghai Bank considered the situation in mid-August so desperate, largely due to speculation by individuals with Government backing operating in opposition to the Government banks, which had been supporting the market against devaluation and were over sold, that on the 27th July he proposed to the head manager that assistance should take the form of a loan to the three Government banks against their promissory notes (backed by the Government), which would be an interbank transaction not requiring Treasury sanction. This being unacceptable, the Ministry of Finance offered the 5 per cent. Customs Revenue Surtax as security for a temporary local loan to be merged in any larger scheme subsequently approved.
- 236. The Hong Kong and Shanghai Bank were informed towards the end of August that His Majesty's Government could approve neither a sterling loan nor even a loan in Chinese currency, which would encroach on the security available for larger schemes, and that they dissociated themselves entirely from the bank's proposals for a palliative loan.
- 237. The attitude of His Majesty's Government at this time was that China should abandon silver and adopt a foreign currency basis, the note issue becoming the monopoly of the Central Bank, the sale abroad of the silver thus released providing reserve to prevent collapse of the currency. If China went on a sterling basis, which appeared best suited to China's needs, His Majesty's Government would help her to obtain loans or credit to back the currency reform scheme, provided: the scheme had the goodwill of Japan, the United States of America and France; the security, including maintenance of the customs administration under a British Inspector-General were adequate; control of the proceeds for currency reform purposes only were assured; reform of Central Bank under a British adviser; re-establishment of Chinese credit, including steps to remedy defaults; and reform of the budget. The best chance of getting such a scheme accepted was to leave the financial crisis to develop.
- 238. The Japanese Vice-Minister of Finance at Tokyo on the 8th August expressed to the commercial secretary at His Majesty's Embassy the view that it would be useless to offer a loan to China for currency reform because she would never consent to essential foreign control. The impression he gave was that Japan was indifferent to China's financial difficulties, sceptical of financial assistance to China in any form, and antagonistic to an international loan.
- 239. Sir Frederick Leith-Ross reached Japan early in September and discussed the situation fully with the high authorities concerned; the Japanese view, as had been anticipated, generally was that foreign help to China was nadvisable and not essential; that China would be unlikely to abandon silver; that China would not accept effective foreign control, so that any loan would be wasted; and that recognition by China of Manchukuo would be no inducement to Japan to change her attitude.
- 240. On arrival in China on the 21st September Sir Frederick Leith-Ross, who was duly welcomed by the Chinese authorities, proceeded to discuss with them the conditions on which foreign co-operation might be possible. He emphasised that reforms would be required (such as reorganisation of the Central Bank and

revision of the budget), that adequate security must be forthcoming (which would involve settlement of existing defaults), and that widest co-operation with other Powers was essential, including Japan. The Chinese Government were urged to explore all possibilities of improving their relations with Japan, and in this connexion it was informally suggested that the recognition of Manchukuo, against adequate compensation, should not be excluded. The general reaction was not to reject the idea as impossible, provided Japan showed any willingness to respond.

- 241. Technical discussions followed, from which it appeared that the Chinese proposed: to concentrate note issue reserves with the Central Bank (the Banks of China and Communications continuing temporarily to issue notes), notes being issued and retired against purchases and sales of foreign currency, and a reserve maintained of 50 per cent. against notes plus sight deposits; to make the Central Bank as independent as possible of the Government by marketing a proportion of the shares; and perhaps to appoint a foreign technical central banking expert in a purely advisory capacity; the budget position was unsatisfactory, owing to heavy military expenditure and domestic loan charges, but it was hoped to balance it in eighteen months; to maintain the export tax on silver (or impose an embargo) and to nationalise all silver in the country; and to deal with tightness of credit and other banking difficulties by creating, inter alia, a special mortgage institution. It appeared that China had an understanding with the United States Treasury that the latter would buy a portion of her silver at current prices; and that she also had considerable though fluctuating foreign exchange reserves. The Chinese requested a foreign loan to put this scheme into immediate effect, though T. V. Soong did not consider a loan essential. His Majesty's Government had from the outset contemplated that such a request would be put forward and were prepared to facilitate the issue of a loan of, say, £10 million in Shanghai under appropriate conditions; but the Chinese were warned that, apart from technical considerations, guarantees would be required as to the maintenance of the present customs administration, and that some action would be taken to settle debt defaults (such as that on the Tientsin-Pukow and Hukuang Loans).
- 242 While details of this proposal were being considered, with particular reference to the position which would arise in the event of active Japanese opposition, the Chinese took action (mainly because the financial situation rapidly deteriorated).
- 243. Meanwhile, in connexion with the settlement of old debts, the Governor of the Bank of England on the 1st November set up a committee in London to negotiate, if necessary, on behalf of bondholders of Chinese Government, railway, and other loans.
- 244. On the 2nd November, 1935, the exchange rate had fallen to 1s. 3d., a run on the banks was anticipated, and it was necessary for the Government to announce a definite policy and to use its resources to maintain the currency at the level which it considered economically sound. It had become generally recognised that financial support would not be available for palliative measures, which would not suffice to break the vicious circle of financial and economic depression, that some basis of currency other than silver must be found corresponding with the internal price level and free from the risk of constant fluctuation; and that this involved the replacement of silver by a foreign exchange standard. On Sunday, the 3rd November, when the banks were closed, the Government announced the adoption of a managed currency, the nationalisation of silver, and measures to make the notes of the three Government banks inconvertible legal tender. It was stated at the same time that the Central Bank would be reorganised as an independent Central Reserve Bank, owned principally by the banks and the general public, and devoting itself to maintaining the stability of the currency; that a special institution to deal exclusively with mortgage business would be created; and that plans had been completed whereby the national budget would be balanced within eighteen months. It was also stated that measures would be taken to prevent unwarranted increases in prices.
- 245 It was hoped that the maintenance of a foreign exchange standard at the proper economic level would lead to a rapid improvement in the adverse balance of payments, thus relieving the financial stringency; the banks would be able to make fresh advances, some rise in commodity prices might occur, budget

revenues would expand, and the value of Government bonds would improve; the process could be facilitated by the sale abroad of silver reserves, the profits on which would increase the resources at the disposal of the Central Reserve Bank and make funds available to the Government.

- 246. These measures of currency reform, which depended for their success on the ability of the Government to maintain confidence in the currency, were accepted and, indeed, welcomed throughout the area in which the Government exercised unimpeded control. The restriction of the note issue to the three Government banks met with the general approval of the business community, though local objections were raised in regard to the concentration of silver reserves at Shanghai. To meet these objections local sub-treasuries of the Currency Reserve Board, set up in Shanghai on the 3rd November to take into safe custody the note issue reserves of the banks, have been created in the principal provincial financial centres, though it is uncertain to what extent silver surrendered to the local boards is under the control of the Central Board. The Peking and Tientsin branch boards appear to be under the control of representatives of the Four Banks' Joint Treasury, who are generally credited with pro-Japanese proclivities. In Kwangtung the Provincial Government applied the Central Government decree for the nationalisation of silver, but exchanged the silver for Provincial Bank notes and entrusted the silver reserves to a local Currency Reserve Board, which at present has no connexion with or responsibility to the Currency Reserve Board at Shanghai.
- 247. The change in the basis of the dollar from silver to a managed foreign currency has, moreover, caused an appreciation in the value of the copper coinage, accentuated by hoarding, which has created some difficulties. These difficulties were temporary and largely due to price-manipulation, especially in North China; steps have, however, been taken to alleviate this situation by the temporary issue of "copper notes" and by the minting of new copper and nickel subsidiary coins to the dollar, "to be issued on the strict basis of decimals of the dollar." A disproportionate rise in the price of commodities in some areas, which followed the fall of the dollar, led to the formation of "price-fixing" bodies by the local authorities, which appear to have operated without causing serious complaint. The general effect on business of the currency reform was distinctly favourable and the export trade, in particular, expanded considerably, as was to be expected, in response to the lower exchange level of the Shanghai dollar.
- 248. On the 16th November the Ministry of Finance issued regulations enjoining the exchange of silver for legal tender notes, which appear to have been accepted throughout the country without arousing opposition. A shortage of currency due to the surrender of coin is being made good by the distribution of new notes through the three Government banks. Distribution in North China is to be effected by the newly-opened Peking branch of the Manufacturers' Bank of China, of which the present Minister of Finance is chairman and T. L. Soong (brother of T. V. Soong) is general manager.
- 249. In mid-December considerable uneasiness was felt in financial circles owing to the change which then took place in the silver-purchasing policy of the United States of America. At that time it was not generally known that any sale of silver by China to the United States of America had been effected, and with the fall in the price of silver doubts were expressed as to whether the Chinese Government would have sufficient reserves of foreign currency to maintain the rate of exchange of 1s. $2\frac{1}{2}d$.
- 250. On the 20th December the Central Bank announced that large quantities of silver had been sold to America to provide additional reserves for exchange stabilisation; a further large shipment was made on the 24th December.
- 251. These two shipments represented together a sale to the United States Government of 50 million fine ounces at 65 United States cents an ounce, which had been completed some weeks previously.
- 252. On the 29th December the Ministry of Finance issued instructions to the China Development Finance Corporation (see paragraph 184 of annual report, 1934) to make preparations for the establishment of a special bank, to handle mortgage business on immovable properties. In this connexion plans have been

considered—without definite result so far—to devise measures to amend the Chinese law relating to mortgages in order to facilitate the enforcement of the rights of the mortgagee.

- 253. On the 31st December it was announced that, on instructions from the Ministry of Finance, the Central Bank of China had decided to set aside 40 million dollars (subsequently increased to 60 million dollars) out of its capital of 100 million dollars for private subscription; it was further reported that a definite decision had been reached for the reorganisation of the Central Bank of China as a Central Reserve Bank.
- 254. The measures of monetary reform were taken by the Chinese Government on their own initiative, but they closely corresponded with the views which had been expressed by Sir Frederick Leith-Ross. His Majesty's Ambassador immediately issued regulations prohibiting British subjects from making payments in silver of the whole, or part, of any debt or other obligation, and the measures have met with little or no opposition from British sources. The debentures issued by certain British companies contain a "silver clause," e.g., a provision that if no coin is available payment under the debenture shall be made in legal tender for the amount of the cost of the equivalent weight of silver; in spite of some opposition, the debenture-holders of the companies concerned have, however, in cases where payments have fallen due, passed resolutions that payment be accepted in legal tender notes.
- 255. It is expected that negotiation of the terms upon which the British and other foreign banks in Shanghai will surrender their silver holdings will shortly be concluded. (N.B.—The foreign banks (with the exception of the Japanese) agreed to surrender their silver early in January 1936.)
- The smooth working of the currency reform measures has been impeded by an active campaign of propaganda conducted by the Japanese press and inspired by the Japanese military, who, assuming that these measures were dictated by Sir Frederick Leith-Ross and that they were backed by a British loan, have chosen to seen in them an attack on the paramount position in China which Japan has arrogated to herself. In North China the Japanese military authorities have deliberately incited and supported "autonomist" movements of a purely artificial character, and they have announced that these movements will result in a separation of the northern provinces and the retention of the revenues collected locally. The East Hopei Autonomous Council, set up with Japanese support, has seized the local salt revenues and has attempted to appropriate the consolidated tax, though apparently no steps have yet been taken to hold customs revenues. Meanwhile, entirely unrestricted large-scale smuggling into China, especially North China, by Japanese and Koreans, with whom the Chinese authorities are not permitted to interfere, has further tended to undermine that general confidence in the finances and currency of the country, on which the success of these measures of reform primarily depend. Towards the end of November, however, the Japanese authorities took steps to prevent the clandestine export of silver by their nationals, which had hitherto been unrestricted. Apart from any question of amour-propre, or of machiavellian designs based on the disintegration of China, which may account in some measure for active manifestations of hostility on the part of the Japanese military authorities, the Japanese attitude towards the loan proposals, and the currency reforms which were complementary, has all along been that internal administrative reform in China and the settlement of her already existing domestic and international indebtedness must precede any new lending; that a loan for currency reform purposes is unnecessary and impracticable; and, further, that any loan now made would not wholly be used for currency purposes and would merely serve to enrich personally and to strengthen politically the anti-Japanese "Sung dynasty," which stands as the present Government of China. Few, if any, foreign observers in China would be prepared to assert that this attitude is without some justification. The persistent distrust which the Japanese have for M. Monnet and the China Development Finance Corporation has also probably been a contributing factor to their hostility.
- 257. There is reason to suppose, in spite of official denials, that the Japanese made proposals in January for the provision of credits in Japan involving a "yen bloc" and a reduction of the Chinese import tariff on Japanese goods to compensate for the necessary devaluation of the dollar. Towards the end of the

year, and probably unconnected with any such previous proposals, Japanese merchants in Shanghai and Hankow have endeavoured to establish the local use of yen as currency for certain purposes. It appears, moreover, from statements made by various high Chinese authorities, that the Japanese have, on more than one occasion, and as late as August, made proposals for a Japanese loan or credit independently of other Powers.

- 258. In view of the separatist movement in North China, and other possible reactions to Japanese activities tending to the disintegration of China, His Majesty's Government decided towards the end of December to allow the loan proposal to remain in the background and to concentrate on questions of administrative reforms, and the settlement of defaults. The French and the American Governments have never displayed any active interest in the loan proposal. The Japanese Government have made it clear that it views any such proposal with the strongest disfavour. His Majesty's Government have consistently maintained the position that there can be no satisfactory solution of China's difficulties without the friendly co-operation of all countries concerned, especially Japan. In the circumstances it seems improbable that any loan, British or international, will be made, and that our immediate object must be to extricate ourselves from the negotiations without too obvious an admission of the fact that we have been forced to abandon the project owing to Japanese opposition which we are not in a position to resist.
- 259. A communication to the other interested foreign Government is under consideration to the effect that: provided the Chinese Government is able to carry out the necessary internal reforms, the inception of which has already been announced, and provided its authoritiy is not undermined by external intervention, there would appear to be no reason why the measures taken should not be successfully maintained and the economic reconstruction of the country eventually achieved by China herself without foreign aid; progress, however, would be greatly accelerated with the support of a foreign long-term loan, which would strengthen the foreign exchange resources of the Central Bank and also cover the budget deficit during the transitional period until income and expenditure can be balanced; the terms upon which the countries which are principally interested in China, especially the United Kingdom, Japan, the United States of America and France, might participate in such a loan of not less than £10 million issued through the foreign banks at Shanghai are submitted for consideration.

VII.—TAXATION.

- 260. According to statements published from time to time by the semi-official news agencies, progress continues to be made with the abolition of miscellaneous exorbitant local levies, the readjustment of farm taxation, and some success appears to have been achieved in the control of provincial and district taxation (see annual report 1934, paragraph 191). With regard to the latter, measures have been passed, and it stated widely complied with, by which local budgets must be submitted to higher authorities, after approval by whom no additional taxation is to be levied, provision being also made for public protest in the event of irregularities.
- 261. The consolidated tax system has been widened during the year and has operated without giving reasonable grounds of complaint, and also without interference, except in the "autonomous" area in Hopei in the closing months of the year. Apart from this limited interference, the Bureaux at Peking, Hankow, Shanghai, and Tsingtao, have been effectively in charge of the Internal Revenue Administration under the Ministry of Finance at Nanking, to which the revenues collected have been paid, though in some cases (e.g., Shansi), the Central Government is compelled to grant a partial refund in the form of a subsidy. In Fukien, Kwangtung, and Kwangsi, which are in theory under the Canton Bureau, the provincial authorities have continued to enjoy wide latitude and have, in fact, done what they chose. Kailan Mining Administration coal came under the consolidated tax in 1934, and this arrangement has since been extended to most of the principal coal mines under the control of the Peking Bureau; during the past year alcohol has also been included in the system through-

out China. Since the 1st August, 1935, the system, with temporary administrative modifications, has been extended to Szechuan, Shensi, Ninghsia, and to Kansu (so far as tobacco is concerned).

262. A moderate tax on exchange transactions in stock and commodity exchanges was promulgated and enforced in May, but not put into operation, owing to strenuous opposition by influential native speculators. Plans were made for the levy of an income tax as from the 1st January, 1936, but no legislation for its enforcement has been issued, and it seems probable that its introduction will be further delayed.

263. "Illegal" taxation in Hunan, Kwangtung (see also for taxation on sugar and chemical fertilisers the section on trade), Kiangsi (see also for the "oil monopoly" the section on trade), Fukien, and Szechuan, has continued to be levied (see paragraph 195 of annual report 1934). In Kwangtung His Majesty's consul-general succeeded in obtaining exemption for goods manufactured in Shanghai by the China Printing and Finishing Company (see paragraph 222 of annual report 1934), and by the Central Agency (Limited), from the special tax levied there on "foreign goods" (see *idem*, paragraph 216). For the position regarding taxation of artificial fertilisers in Kwangtung, see the section on trade.

264. British subjects have been advised to pay municipal house taxes at Shanghai and Peitaiho, and a restaurant tax at Nanking.

The new Stamp Tax Law, promulgated in December 1934 and enforced on the 1st September, 1935, omitted the objectionable provisions of the old regulations for a consumption tax on wines, spirits, and aerated water (though the former tax on the last-named is still temporarily sanctioned). The new law has called for no modification of the advice hitherto given to British subjects to affix stamps at the rates laid down (or to cause such stamps to be affixed) on such documents as are likely to come under the cognizance of the Chinese authorities. This advice now specifically includes insurance policies. American citizens are told by their national authorities that the expediency of affixing revenue stamps is left to their individual judgment and that of their Chinese business connexions. The Japanese authorities are resisting the application of the law. The French Legation has informed the Waichiaopu that the law is inapplicable to French citizens. On the part of other Powers there appears to be a general agreement on the attitude adopted by ourselves and the Americans. On the 23rd August the Waichiaopu forwarded a copy of the law, with the request that British subjects be instructed to comply with its provisions. Messrs. Butterfield and Swire complained that the law discriminated in favour of Government-owned enterprises, since these are exempted from affixing stamps to go-down warrants, storage receipts, bills of lading, and insurance policies. The principle involved being important, though the stamp duties in question were small, His Majesty's Ambassador on the 18th September orally drew the attention of the Waichiaopu to this point, and put the suggestion (made by Messrs. Butterfield and Swire) that, if the discriminatory clauses were not cancelled, the responsibility for affixing stamps should be transferred from the issuer to the recipient of the document. Similar complaints have since been made by the British Chamber of Commerce at Shanghai and the Shanghai General Chamber of Commerce through the senior consul; these bodies have objected also to the multiplicity of documents which require to be stamped, and to an alleged excessive amount of the tax on bills of lading. It is understood that the Chinese authorities are considering amendments of the rates in force which would obviate these objections from a practical point of view. The question of an agreement for the enforcement of the law on Chinese in the International Settlement at Shanghai is under consideration. Chungking and at Nanking payment of the stamp tax on cheques drawn on the official accounts of His Majesty's consular officers has been avoided by drawing cheques on their accounts with the Hong Kong and Shanghai Bank at Shanghai. At Swatow a similar demand made by the Bank of China in September has not so far been persisted in. The tax, even if fully enforced, seems unlikely to prove a serious burden to British trade.

266 The business tax has not been discussed with the Chinese authorities in the course of the year, though it is apparently being paid generally by Chinese over a considerable portion of the country; the whole question has been carefully

reviewed in this Embassy and in the Foreign Office, and is being considered by a special sub-committee of the Joint Committee at Shanghai of the British Chamber of Commerce and the Chinese Association, from the point of view of practical objections to payment by British subjects (see paragraph 190 of annual report 1934).

267. A consolidated tax on alcohol in the nature of an excise replaced former taxes as from the 1st January, 1935, and arrangements were made for the collection by the customs of a similar tax on imported alcohol in addition to import duty. No undue burden was placed on goods of British origin, and the tax (which was considerably lower than those previously in force) was analogous to existing taxation on tobacco, cement, and other goods. The consular body at Shanghai represented through the senior Minister that collection through the customs was an infringement of treaty rights, a contention in which this Embassy and the Foreign Office did not concur. The senior consul reminded the Internal Revenue Administration that such taxation could only be imposed in foreign concessions and settlements by agreement with the authorities concerned. Messrs. Liddell Brothers have an interest in an American distillery in the Settlement at Shanghai, and are (or were) considering the erection of another in the British Concession at Tientsin. Messrs. Slowe and Co. contended that in practice the imposition on imported alcohol of the new tax, in addition to the already very high import duties which had seriously checked imports (the former taxes not having been paid on alcohol consumed inside the Settlement and having been widely evaded outside), had rendered it impossible to continue importing alcohol from Java in competition with the local product. It was decided, with Foreign Office approval, that there were no reasonable grounds for any representations to the Chinese authorities. (For particulars of the China National Distilling Company, see section on trade.)

268. In connexion with an attack on the hand-rolled cigarette industry (see the section on trade), the British-American Tobacco Company have stated that they hold the present rates to be discriminatory and have suggested that the rates be equalised: the attention of the Chinese authorities has been called to this aspect of the question, which has, however, not been fought on these lines. There have been no actual modifications of the consolidated tax on rolled tobacco (see annual report 1934, paragraph 189).

VIII.—TRADE.

269. Except in North China, and there principally in the last quarter of the year (see sections on Japanese political and economic activities), trade has been less hampered than usual by political unrest, though Communists have still been active in the remoter and more inaccessible districts of North-Western Szechuan, Northern Hunnan and Northern Shensi, while the mountainous areas of Fukien and Kiangsi are not yet clear of scattered bands of marauders. The principal difficulties of an economic nature which merchants have had to face have been those of currency and exchange (see section on finance). Devastating floods in Southern Shantung, Northern Kiangsu, parts of Hupei, and elsewhere, have caused losses amounting to many million dollars, and have seriously disorganised markets in the interior.

270. A remarkable increase in smuggling has also prejudiced legitimate trade.

271. Total customs revenues in 1935 (as compared with 1934 and 1933) were approximately as follows:—

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		(In m	(In millions of do	
Import duty	 	265.6	260.2	250.3
Export duty	 	23.3	24.7	20.6
Interport duty	 	18.0	16.9	13.2
Tonnage dues	 	4.4	4.3	4.3
Flood surtax	 	14.1	14.3	13.6
Revenue surtax	 	14.1	14.2	13.5
Totals	 	339.5	334.6	315.5

- 272. The increase in the import duties in July 1934 (see annual report 1934, paragraphs 242–43) has masked the decline in the volume of import trade in 1935 as compared with the previous years. Apart from silver, exports show an increase of approximately 2.7 per cent. The apparent adverse balance of trade has been reduced from 74.84 million dollars in 1934 to 48.77 million dollars in 1935. Owing to smuggling, and to elimination from the returns of records of imports of munitions, the actual adverse balance is certainly very much greater. Such genuine adjustment of the balance as has occurred has been due more to China's inability to pay for imports than to any considerable increase of exports. The high value of the dollar in terms of foreign currencies during the greater part of the year and continued depression abroad have probably prevented any substantial remittances from Chinese overseas, and there has been no important investment of foreign capital. It may be noted, however, that, for the first time, the December returns showed a favourable balance of trade.
- 273. Proposals for tariff adjustments to encourage exports, protect native industries, and discourage imports without diminishing revenues, are described in the customs section of this report.
- 274. Among other measures to adjust the adverse balance of trade, and so reduce China's adverse balance of payments, which have been under serious consideration by the Chinese Government, have been means to make China self-sufficient in her food supplies. Plans, comprehensive though not yet concrete, are under consideration, and partially in operation, with regard to supplies of rice, cotton and wheat. In connexion with these schemes, public granaries are to be set up, with a view to their operation by the co-operative societies, throughout China. In commenting on these proposals in an article published in the *China Economic Journal* in August 1935, the Minister of Industries adumbrated measures to compel Chinese rice merchants to start an annual increase of 10 per cent. in purchase of native rice, so that by the end of ten years there would be no more imported rice, and Chinese millers to make a similar annual increase in the purchase of Chinese wheat.
- 275. Meanwhile, progress has been made in lightening the burden of taxation in rural districts, in the extension (perhaps too rapid) of co-operative credit societies in the villages, in the promotion of cottage industries, in afforestation, and in endeavours by irrigation and other means to bring new land under cultivation. Apprehensions that the co-operative movement may develop on lines prejudicial to foreign trade; the manner in which the regulations for the proper control of fertilizers have been administered primarily for purposes of taxation and for the protection of the native product; and the discrimination in favour of hand-rolled cigarettes, are described in subsequent paragraphs. The National Economic Council's Commission for the Improvement of the Sericultural Industry has distributed during the year several millions of selected mulberry trees, and cards of silkworm eggs at nominal prices, and sericultural advisory stations have been opened in the chief producing centres. Extensive experiments have also been made with American cotton seed.
- 276. The extension and improvement of communications by rail and road, which have been rapidly and uninterruptedly pressed forward mainly for strategic reasons, are doing much to open up the countryside to new markets for rural produce.
- 277. A scheme under which the services of six British agricultural experts, to be attached to the National Agricultural Research Bureau, should be financed from British Boxer funds is under consideration.
- 278. The Ceylon Government, though constrained to refuse facilities to Chinese students at the Ceylon Tea Research Institute, have arranged for a representative of the National Economic Council to inspect the cultivation and manufacture of tea in the colony.
- 279. The Government Testing Bureaux have continued to function and have enlarged the scope of their activities without serious complaint from British exporters, who, however, consider the bureaux useless and irksome.
- 280. Nevertheless, though rural rehabilitation has become a popular panacea for all China's economic ills, industrial development has not been neglected.

- 281. A large increase in the production of native cotton in 1934 has not resulted in any improvement in the condition of the Chinese cotton textile industry. On the 28th December, 1934, the National Government issued general, but vague, instructions to relieve the industry, including cheap loans, modification of customs and excise duties, control of production, and sumptuary regulations; but no steps were taken to put them into effect, and in February the Minister of Industry stated that the causes of depression in the cotton textile industry were too complicated to be dealt with in this manner. The Sung Sing Cotton Spinning and Weaving Company, one of the largest industrial units in China, which owns nine cotton mills, has long been in serious financial difficulties. The Hong Kong and Shanghai Bank, who hold a first (legal) mortgage on No. 7 mill for a loan of 2 million dollars, which has long been in default, and who hold also the title deeds transferred into their name when the mortgage was made, published a notice in February of their intention to foreclose, setting a reserve price of 2,250,000 dollars. Chinese banks holding a second mortgage for 2,800,000 dollars on the same property immediately obtained from the First Special District Court an order of attachment for the whole property. The property was put up to auction on the 26th February and knocked down to a Japanese, who was, in fact, however, acting secretly on behalf of the bank. Meanwhile, the district court had requested His Majesty's consul-general to instruct the British auctioneers to postpone the auction and the Hong Kong and Shanghai Bank to abstain from transferring the property: a request which he had no option but to refuse. The mayor, on instructions from the Executive Yuan, then intervened in an endeavour to arrive at a settlement, but the terms were refused by the bank. No agreement has yet been reached, but in the correspondence which ensued two points have been emphasised which are fundamental in the system of credit on which the commercial, industrial and financial prosperity of Shanghai are based: First, that land held on the British register of titles can now only be transferred with the concurrence of the Chinese Land Bureau; secondly, that the Chinese authorities maintain that such cases are governed by Chinese law, which voids any agreement stipulating that the ownership of mortgaged property automatically passes on default. (In this connexion, see also under the shipping section of this report the paragraphs relating to the indebtedness of the China Merchants' Steamship Navigation Company to the Hong Kong and Shanghai Bank.)
- 282. This whole question of the disabilities under which creditors suffer in Chinese law when endeavouring to realise on property pledged as security for credit facilities has become a matter of prime importance in connexion with the financial crises in Shanghai, where the resources of the banks are largely locked up in unrealisable real estate. A number of proposals for a solution of the problem have been put forward, but no effective steps have yet been taken to remedy the situation.
- 283. The China Alcohol Distilling Company, a unit in the State industrial plan (see annual report 1934, paragraph 208), though a joint enterprise of the Ministry of Industry and a group of overseas Chinese merchants, commenced operations in January 1935, and has, under the Law for the Encouragement of Industrial Enterprises (see annual report 1934, paragraph 215), been granted rights of monopoly manufacture in Kiangsu, Chekiang and Anhui, the declared object being to prevent cut-throat competition from new ill-conceived mushroom distilleries erected to snatch a quick profit from a new industry regardless of the needs of the market (see paragraph relating to the new consolidated tax on alcohol in the taxation section of this report).
- 284. The erection of the Central Machine Works, at Chenju, near Shanghai, was commenced in January, the British Boxer trustees having advanced 200,000 dollars for land, &c., and 123,000 dollars for purchase of machinery in England.
- 285. Projects for the formation of a match monopoly, which were known to be under consideration early in 1935, were revived in October in the form of a proposal for a Sino-Japanese joint production and sales organisation which would amount to a monopoly. The possibility of joint representations on behalf of Swedish, American and British interests in match production in China is under consideration.

286. In January 1935 it was learned that Japanese were pressing strongly to obtain a contract to construct waterworks at Macao, and it was obvious that their proposals embraced wider schemes, unwelcome to the Portuguese and threatening to British interests in those regions. On the 17th July, 1935, however, a contract was signed by Malcolm and Co. (Limited), of Shanghai, with the Macao Waterworks Company (Limited) (a newly formed Hong Kong British company, "holding" the Portuguese Macao Waterworks Company) to construct the new waterworks at Macao at a price of 1,474,000 Hong Kong dollars and to purchase the existing waterworks. The Hong Kong and Shanghai Bank financed the scheme to the extent of 2 million Hong Kong dollars and, having been pressed by the service representatives in the colony to forestall the efforts of the Japanese, have requested a guarantee from His Majesty's Government in the United Kingdom for protection in case of political interference.

287. Restrictions imposed on and regulations controlling the supply of electricity in Macao, which were alleged seriously to affect the business of the Macao Electric Light Company, has formed the subject of correspondence between His Majesty's consul-general at Canton, this Embassy and the Foreign Office, into whose hands the question has now passed.

288. In Kwangtung progress continues to be made with the industrialisation schemes of the Provincial Government, in spite of financial difficulties (see annual report 1934, paragraph 213). In addition to sugar, cement and fertilisers, the Sales Management Office for the Products of Provincial Factories has marketed considerable quantities of piece-goods and wolfram ore (the last named having, however, now been placed under the control of the Military Industrial and Development Department). The alcohol distillery has been completed, and paper works, a brewery and an aerated water factory are in course of construction. Messrs. Reiss Massey and Co. have obtained the contract to erect a jute factory in Southern Kwangtung at a price of £30,000, and a further contract for the power plant and electrical equipment to the value of £9,400. Messrs. Malcolm and Co. are likely to secure, in face of German competition, the contract for a new waterworks for Canton, provided British Boxer funds are available. In February tenders were called for additional machinery for the Kwangtung Spinning and Weaving Works.

The project for the construction of the Kwangtung Iron and Steel Works is still under negotiation by Messrs. Brassert and Co. in conjunction with other British firms (see annual report 1934, paragraph 229). In February 1935 the Minister of Industries and the Vice-Minister for Foreign Affairs at Nanking informed His Majesty's Minister's representative that the Central Government had no objection to the scheme in principle, but that in view of the poor quality of the iron-ore and the long haul for coal, the proposed site and available raw materials should be resurveyed. In March the Hong Kong and Shanghai Bank agreed in principle to participate (provided 50 per cent. was paid by the Kwangtung Government before completion) up to limit of £200,000, subject to the unequivocal consent of the National Government and to participation to an equal amount by the Exports Credit Guarantee Department. In April the Vice-Minister for Foreign Affairs at Nanking informed the Chinese counsellor of this Embassy that the Central Government authorities would expect to be consulted as to the details of any contract, which would, moreover, require their approval. After consultation with the China representative of the British group the Exports Credit Guarantee Department expressed the opinion that the moment was inopportune for the scheme. Meanwhile, the American group were still negotiating, and an offer was made by Skoda. On the 26th July, 1935, Sir Frederick Leith-Ross, and representatives of the Board of Trade, the Export Credits Guarantee Department and the Treasury, discussed the scheme with representatives of the British group. Sir Frederick Leith-Ross stated that the existing financial and economic situation in China seemed extremely unsatisfactory. He thought that, if after his arrival in China he saw hopes of improvement, the scheme should be encouraged. The Board of Trade representative said these large orders for plant in China would be welcome if prospects of payment were reasonably sound, since British exporters of iron and steel would not be seriously prejudiced. The China representative of the group has since returned to China and is pursuing the negotiations.

- 290. The contract for the Chien Tang River Bridge (see annual report 1934, paragraph 229) was, as anticipated, eventually given to Dorman Long and Associates, and accepted on terms which they considered satisfactory.
- 291. Considerable progress appears to have been made in Shensi Province, especially in irrigation, afforestation, promotion of rural co-operative societies, and the construction of motor roads. The extension of the Lunghai Railway to Sian in December 1934 has already promoted commercial activity and a number of modern banks have been opened.
- 292. In spite of threats of economic Japanese penetration, and the activities of Communist bands, which have combined to drive Shansi into closer touch with Nanking, the province maintains its economic isolation (see annual report 1934, paragraph 216). The completion of the southern section of the Tatung–Puchow light railway has stimulated exports and improved trade generally. The industrial development of the province has been in the hands of the Germans and Japanese (possibly working in conjunction). Cigarette, cotton, cement and powder factories, and an arsenal, machine shop, steel works and flour mills, are now in operation. The finances of the province are, however, in a parlous state, and it is believed that all this equipment has been supplied at very low prices and on long credit.
- 293. There has been no actual investment of British capital in Kwangsi (see annual report 1934, paragraph 227), but British, as well as Japanese and Singapore Chinese, interests have made investigation of the possibilities.
- 294. With regard to the Yangtze Corporation and the development of Szechuan (see *idem*), Messrs. George McBain were in June 1935 appointed the agents in China for the corporation, in regard, *inter alia*, to the latter's rights arising out of the Pritchard Morgan mining concessions of 1898 and 1899. Meanwhile, the corporation appears to have negotiated in London in June, through other parties, an agreement with an Yihwa Company, purporting to act on behalf of the Szechuan authorities, for the organisation of a company to develop mining properties, &c., throughout the province.
- 295. A note on the native mining industry is contained in the mining section of this report.
- 296. Grants of "rewards" continue to be made to Chinese citizens and companies under both the Law for Encouragement of Industrial Technique and also the Law for the Encouragement of Industrial Enterprises (see annual report 1934, paragraph 215). The French, American and Italian representatives have made formal reservation of treaty rights which might be infringed by the operation of the Law for the Encouragement of Industrial Enterprises; in December 1934 the Japanese Minister informed the doyen that he was prepared to protest against the operation of the law. In November 1935 rights of monopoly manufacture having been granted in July to two Chinese factories in respect of cigarette paper, and the British American Tobacco Company having stated that they contemplated producing cigarette paper for their own use and also possibly for sale, His Majesty's Ambassador drew the attention of the Ministry for Foreign Affairs to the infraction of His Majesty's Government's treaty right, which would be involved were British subjects to establish factories in the districts concerned for the manufacture of similar goods, and any attempt made to prevent them from doing so on the grounds that exclusive rights of manufacture had already been granted under the law in question.
- 297. In July 1935 instructions were issued by the Customs Revenue Department that sugar below 98 degrees polarisation, imported into Canton to be processed by the Kwangtung Government provincial sugar mills, should pay import duty at Shanghai, half the duty being deducted from a deposit in the Bank of China at Shanghai, the remaining half duty being recorded for subsequent collection and entry in the revenue account as duty leviable, but not yet paid. Pending an agreement as to the handing over by the Kwangtung authorities to the customs of the collection of the tax on foreign rice, 50,000 quintals of sugar were to be allowed to be imported by the mills on these conditions before the 1st September: by that date only 20,000 quintals had been so imported, and the Canton Government had not fulfilled its part of the bargain, nevertheless the

customs were instructed to allow the remaining 30,000 quintals to be imported on the same terms, and some sugar imported by the mills, which was over 98 degrees polarisation, was allowed to be imported on paying duty in the manner provided by the agreement at the rate for sugar under 98 degrees polarisation. As it has so far been impossible to state decisively that the sugar imported by the mills under this exceptionally favourable duty paying treatment, was, in fact, of the same grade as sugar imported by British firms, representations, which were made to the Waichiaopu by His Majesty's Ambassador on the 28th October, were confined to a request for an assurance that terms not less favourable than those on which the Kwangtung Sugar Monopoly are being allowed to pay import duty on raw sugar will also be granted to any British firms which may import similar sugar of the same origin. Owing presumably to bad management and "squeeze" on the part of the Kwangtung mills, the imports into other parts of China of sugar processed by the Canton mills has not, in fact, seriously affected imports of sugar from abroad by foreign firms. The whole of the output of the Canton mills is exported for sale in other provinces. Meanwhile, the Canton Sugar Monopoly, who act as sole importers of sugar of all kinds for consumption in the province, have imported considerable quantities of sugar from abroad, including sugar refined in Hong Kong by Messrs. Butterfield and Swire, who have it is understood little to complain of in so far as the amount of the sales is concerned, though they object to the methods by which the monopoly controls the supply of all sugar in the province.

298. Since the end of 1934 imports of foreign cement into Kwangtung are only passed by the customs if accompanied by permits issued by the Kwangtung Native Goods Sales Office on the recommendation of the Provincial Reconstruction Bureau.

In February the Director of the Bureau of Agriculture and Forestry of the Kwangtung Provincial Government made an agreement with Imperial Chemical Industries and other importers of chemical fertilisers to secure the abolition of the bureau's tax of 1 dollar a bag for examination, to which the importers had agreed in March 1934, in return for a monthly donation (of half the amount of tax) to the bureau for agricultural purposes. On the same day, however, as the result of instructions of which the director was unaware, a customs notification exempted artificial fertilisers from inspection and labelling by the bureau, and shortly afterwards the press announced that new regulations, amounting to a virtual Government monopoly, had been passed forbidding the sale of sulphate of ammonia and other unmixed fertilisers. Neither the agreement, nor the regulations, were put into force: fertilisers if imported by the firms are still subject to customs duty, the bureau's examination fee, and a "university ; there are no restrictions on the import of unmixed fertilisers, but the provincial government factory enjoys a monopoly, because it imports without payment of duty, fee, or surtax. The factory, however, obtains its supplies from the Imperial Chemical Industries and other foreign importers, and markets them after a purely nominal admixture of other ingredients which are admittedly desirable. In the circumstances, the Imperial Chemical Industries have not requested the intervention of this Embassy.

300 An agreement was come to at the end of 1934 of the terms upon which Messrs. Arnhold and Co. (Limited), might act as sole distributors of the Hunan Antimony Syndicate. Enquiries were made by the American Embassy, and it is believed that protests were made by the Japanese authorities to the Hunan Provincial Government regarding this monopoly. It was decided that there was no occasion for this Embassy to make any formal protest against such an appointment, but that, on the other hand, no official support should be given to the firm. Owing to fluctuations in the world price of antimony the proposed arrangements were eventually cancelled. It is understood that the Hunan Antimony Syndicate is now being reconstituted so as to give the Provincial Government a large share of control

301. Difficulties experienced in the spring of 1934 by the Hankow Dispensary in obtaining supplies of sulphuric acid from Messrs. Major Brothers in Shanghai (see annual report 1934, paragraph 214), were eventually settled by special intervention by the Minister for Foreign Affairs, and the firm were enabled to obtain their supplies on condition that they paid an ad valorem tax of 25 per

cent. to the Hupeh Saltpetre and Sulphuric Acid Bureau, and on the understanding that the arrangement was confined to that consignment only. In December 1934 the dispensary applied for huchaos to import further supplies of acid, which were refused by the bureau. As the result of official representations made by His Majesty's Minister in March, the Ministry of Finance decided in May that all sulphuric acid required by the dispensary for the manufacture of mineral water should be dealt with as a special case, the dispensary being allowed to apply for huchaos and to make their own arrangements for purchase and transport for any quantities they might require, provided the tax of 25 per cent. ad valorem were paid; at the same time the Ministry of Finance maintained that sulphuric and nitric acids, as well as sulphur and saltpetre, being munitions of war, the monopoly arrangement for the control and sale of acids in Hupei by the bureau were necessary. The dispensary expressed themselves satisfied that freedom to choose their suppliers had been given; they purchased their supplies in 1935, in fact, from the bureau, and have found the quality satisfactory and the price virtually the same as that which they would have had to pay the British firm plus the tax.

In January 1935 the rights to levy the tax on sulphur and sulphur products were sold by the Kiangsu Sulphur and Saltpetre Bureau to a new monopolist, who was known to have paid considerably more for the privilege than his predecessor. Notices were issued on the 31st January to the effect that new tax receipts would be issued as from the 1st February and that all consumers of acid on which tax had been paid to the old "farmer" were to register their outstanding stocks with the bureau before the 3rd February. Instead of endeavouring to arrive at a compromise with the new monopolist as they had with the old, Messrs. Major Brothers, in conjunction with their Chinese competitors, refused to recognise him and made joint representations to the Ministries of Industry and Finance and also to the Executive Yuan. Meanwhile, the Chinese police, acting on the behalf of the Monopoly Bureau, prevented acid covered by old tax receipts from leaving the company's works, which were outside settlement limits. As a result, the British company and their Chinese competitors were obliged to make an arrangement whereby they paid the tax under protest direct to the bureau pending settlement of the question. On the 15th April His Majesty's Ambassador addressed a note to the Minister for Foreign Affairs explaining in detail the objectionable features of this monopoly and reminding him that His Majesty's Government regarded the institution of such monopolies as an infringement of their treaty rights. The Minister for Foreign Affairs replied on the 8th May that the institution of these monopolies was designed for purposes of control and the Chinese Government could not admit that they constituted any infringement of the treaties. In July the Kiangsu Sulphur and Saltpetre Bureau was instructed by the Ministry of Finance to remit the total amount of the tax which had been paid under protest by Messrs. Major Brothers; His Majesty's consul-general at Shanghai wrote to the director of the bureau pointing out the objectionable and unequitable features of the tax, and suggesting that when modifications, which the bureau had been instructed to propose, were made in the system these features would be taken due account of. On the 3rd December Messrs. Major Brothers applied through His Majesty's consulgeneral to the bureau for huchaos to cover importation from Formosa of 100,000 kilog. of sulphur. On the 6th December the bureau sent a letter direct to Messrs. Major Brothers instructing them to buy Honan sulphur instead of importing sulphur from abroad, and returned the application forms for alteration accordingly. His Majesty's consul-general thereupon wrote to the bureau pointing out that any form of compulsion on a British company to buy Honan sulphur was an unwarrantable interference with the company's legitimate trade, and requesting that the applications for huchaos be transmitted to the Ministry of Finance without delay.

303. In February 1935 the Kiangsu Saltpetre and Sulphur Bureau, after informal representations by His Majesty's consul-general at Shanghai, agreed to waive a request which they had made to inspect the works of the China Printing and Finishing Company (as users of chlorate of soda).

304. At the end of 1934 regulations were issued for the gradual lifting of the blockade which had been enforced in Kiansi, Anhwei, Fukien and other Communist-infested areas to prevent necessaries, including kerosene, from

reaching the hands of the insurgents (see annual report 1934, paragraph 214). These measures provided for the retention of the blockade in certain areas still disturbed and for the lifting of the blockade in certain other areas, with the exception that kerosene (and salt) was to continue to be distributed only through the Public Sales Bureaux, which had formed an essential feature of the blockade, it being stated that the bureaux were to continue temporarily to function in all districts until an association of co-operative societies had been set up capable of taking over distribution of kerosene and salt. The representatives in Kiangsi of the Asiatic Petroleum Company, and the American oil-distributing companies, feared, apparently with some grounds for their apprehensions, that the co-operative societies would merely perpetuate the monopoly which had been enjoyed by the bureaux. Informal representations were accordingly made to the Waichiaopu, from whom apparently satisfactory assurances were received. It transpired, however, in July that certain Public Sales Bureaux which had been closed in April had been reopened, and His Majesty's consul-general at Hankow protested to the local authorities against the reopening of these bureaux and requested that freedom of trade be restored to the British company and its agents; similar representations were made on behalf of His Majesty's Ambassador at the Waichiaopu on the 3rd October. Early in October the British and American oil companies, in order to bring matters to a head, stopped deliveries to the bureau at Kian, one of the places at which the bureau had been closed and reopened; as the result of this action, the Kwanghua Petroleum Company's agent (a Sino-Soviet organisation) was left in sole possession of the local market and of the bureau, the office of which he transferred to his company's premises. As this virtual monopoly was the result of action taken by the foreign companies, it was felt that it would be unreasonable to protest to the Chinese authorities that the situation was contrary to the monopoly clauses of the treaties, but the attention of the Waichiaopu was drawn to the fact that the foreign companies had been obliged to act as they had done by the intolerable restrictions to which their trade was subjected by the regulations under which the bureau functioned. The American Embassy, making no distinction between Public Sales Bureaux and the co-operative societies, has protested against the operations of both as contrary to treaty. This Embassy, while apprehensive that the co-operative societies, when set up, may, in fact, merely perpetuate the monopoly enjoyed by the bureaux, has been anxious to avoid an unwarranted attack on the co-operative movement as such, since the latter is being established on the advice and with the assistance of representatives of the League of Nations as part of a scheme of rural rehabilitation. Frequent representations which have been made to the Chinese authorities on behalf of the Asiatic Petroleum Company in Kiangsi have therefore been confined to protests against the continued functioning of the Public Sales Bureaux, and to endeavours to obtain assurances that the co-operative societies, when established, will prove unobjectionable in operation. There is so far no conclusive evidence that it is the intention of the Chinese authorities to transfer to the co-operative societies the monopoly privileges of the bureaux, and opportunities have been taken in the course of informal discussions with the head of the League of Nations Office at Nanking and with the new League of Nations Adviser on Co-operatives, to communicate our apprehensions that the co-operative movement may develop on wrong lines and become merely a system for enforcing Government monopolies.

305. In January 1935 the London office of the British American Tobacco Company, at the instigation of the Shanghai office, urged that representations be made against the unfair rates of taxation discriminatory in favour of handrolled cigarettes, competition from which had first begun seriously to be felt in 1931 (see annual report 1934, paragraph 225). This very complicated and difficult question has been the subject of consideration and much correspondence throughout the year (see also section on taxation). After consultation with a representative of the company, His Majesty's Minister in February wrote personally to the Minister of Finance, emphasising the practical aspects of the problem, with special reference to the diminution of business in machine-made cigarettes, and the resultant loss of revenue, attributable to the inequitable advantages enjoyed by hand rollers, but touching only lightly on the legalistic rights of the British company, on the alleged discrimination (by which, in fact, Chinese manufacturers were equally affected), and on the possibility of lowering

the existing high rates of tax on machine-made cigarettes (the arguments for which appeared to be unconvincing and doomed to be ignored). In subsequent discussions which His Majesty's Ambassador held with the Minister of Finance, the latter stressed the necessity for more efficient control of hand rollers and for the stricter prevention of the clandestine sale to them of materials for cigarette making, especially paper; he was opposed to raising the tax on hand rollers as being at once impracticable and inequitable to this cottage industry. This question was also discussed by His Majesty's Ambassador with the Minister for Foreign Affairs. As the result of further correspondence, and of the efforts made by the British American Tobacco Company themselves through the Chinese manufacturers and through their connexions in the Internal Revenue Administration, as well as of representations made by the United States Embassy, who intervened on behalf of American leaf importers, a reply was eventually received from the Minister of Finance at the end of May transmitting a memorandum drawn up by the Internal Revenue Administration suggesting that the Shanghai Municipal Council should agree with the tax authorities on measures to prevent manufacture in the settlement of the raw materials of the hand-rolled industry; that before April 1937 hand rolling should be eliminated, after which cigarette factories should be confined to Shanghai, Hankow, Tientsin and Tsingtao; that, meanwhile, already registered hand rollers be exempt from tax, though their supplies of paper must be obtained from official sources. On the 27th June the British American Tobacco Company wrote to the Internal Tax Administration urging that steps be taken for elimination of hand rolling by the end of 1935, that no exemption of hand rollers from taxation be granted (or, alternatively, that a new reduced rate on machine-made cigarettes be applied equally to hand rolled), and that a special preventive service be established Meanwhile, various orders were issued by the Ministries of Finance and Communications to prevent the sale of raw materials to unregistered hand rollers, and arrangements were made for discussion between the concession and settlement authorities at Shanghai and the Chinese authorities concerned. Taking advantage of the expectations aroused by Sir F. Leith-Ross's arrival (see section on finance), His Majesty's Ambassador once more approached the Minister of Finance on the 28th October. On the 6th December the Executive Yuan granted a petition from the Ministry of Finance requesting that: Local Governments be ordered to prohibit illicit manufacture; that district magistrates enforce suppression on the joint group responsibility system; that the industry meanwhile be restricted to production on wooden machines by already registered rollers in special areas in Shantung, Honan and Anhwei; that only local marketing be permitted; that registered hand rollers be eliminated by lot; and that no further registration of hand rollers be made. Instructions were sent accordingly to all provincial and municipal Governments; the Military Affairs Commission and the Ministry of Railways were requested to collaborate. To what extent these measures will prove effectual remains to be seen, but the company consider them at least a step in the right direction.

306. In January there was a violent recrudescence of the anti-British boycott in Chekiang Province (see annual report 1934, paragraph 221). Wenchow, on the 19th May, a cargo of cigarettes valued at 81,225 dollars, belonging to the British American Tobacco Company, was seized by the local Tobacco and Exchange Shops Association and destroyed; a similar incident occurred on the 1st June at Szean, when the company's cigarettes to the value of 314 dollars were also destroyed. The movement, which threatened at one time to embrace artificial fertilisers imported by Imperial Chemical Industries (Limited) and other British goods, appears to have been principally confined to the goods of the British American Tobacco Company and its subsidiaries. The origins of the agitation this year are obscure: it seems, however, that the movement was initiated by a newly-appointed official, who hoped to ingratiate himself with the authorities, and in particular with Chiang Kai-shek, by demonstrating his active support of the New Life Movement; that, once started, the business rivals of the British American Tobacco Company took advantage of the occasion to increase the agitation against the British company's cigarettes, which had hitherto held the market to the virtual exclusion of their own; that the provincial authorities were themselves inclined to take no active steps to prevent the agitation, partly because they had recently been deprived by the central authorities of a subsidy from the consolidated tax and partly because owing to the provincial adverse balance of trade they were glad to see a check on imports into the province from Shanghai. The agitation has persisted, though within a diminishing area, and with lessening virulence throughout the year, and has not yet entirely ceased. Formal claims were presented by His Majesty's consul-general at Shanghai to the Provincial Government on the 12th July in respect of the losses suffered by destruction of the company's stocks, and copies of these claims were communicated to the Ministry for Foreign Affairs by His Majesty's Ambassador's representative at Nanking on the 22nd August. When the trouble first became serious, His Majesty's consul-general at Shanghai despatched one of His Majesty's vice-consuls on the 30th May to interview the local officials concerned, and to make an official investigation. The matter has been the subject of repeated representations, formal and informal, written and oral, to the provincial and to the Central Government authorities, and His Majesty's Ambassador has invoked the personal intervention of the Minister of Finance and also that of General Chiang Kai-shek. The British American Tobacco Company have also been active on their own behalf, their principal difficulty being the new vested interests which have taken root while they were driven from the field.

307. The Eastern Extension Australasia and China Telegraph Company (Limited) and the other foreign cable companies have had frequent cause of complaint against discrimination in favour of the radio circuits operated by the Department of Telegraphs and Telephones of the Ministry of Communications, owing to non-observance by the offices of the Department (by which the cable companies' messages are transmitted under the agreements concluded in 1933) of routing directions on messages intended to be transmitted by cable, and owing to other methods of unfair discrimination in favour of the Government radio service. The intervention of this Embassy has, however, not been requested.

308. Attempts to force the Tientsin Native City Waterworks (Limited) to reorganise as a Chinese company were pressed in the early part of 1935, but with the increasing dominance of Japan in North China have been dropped (see annual report 1934, paragraph 217, and paragraphs in the mining section of this report relating to the affairs of the Kailan Mining Administration and the Mentoukuo Coal Mining Company).

In May the Bureau of Health of the Municipality of Shanghai issued regulations for the registration of compounded medicines in the municipality. As the result of enquiries made by His Majesty's consul-general at Shanghai, the Director of the National Health Administration informed the chairman of the British Chamber of Commerce in August that those regulations could be ignored, but that it was proposed to enforce, with certain modifications, as from the 1st January, 1936, the rules governing patent and proprietary medicines promulgated on the 26th April, 1930, and the rules governing medicine merchants promulgated on the 24th August, 1929, and he stated that he would be glad to discuss these regulations with interested British firms. Correspondence was subsequently exchanged between the British and other foreign firms concerned, and the Director, as a result of which it became clear early in December that, though certain further modifications were made in the rules, many points remained to which the firms objected, and to which they attached the greatest importance. An oral request was made to the Waichiaopu for an assurance that the operation of the rules had, in fact, as was understood, been definitely postponed until the 30th June, 1936. On the 28th December, His Majesty's Ambassador made formal representations to the Waichiaopu, transmitting a statement embodying the objections which British firms had to the rules in their present form and indicating the results of the informal discussions which had taken place, and he requested that this statement might be conveyed to the competent authorities for their most careful consideration: attention was also drawn to the fact that certain articles of both sets of regulations would, if enforced against British firms, infringe the rights of His Majesty's Government in the United Kingdom under existing treaties: a request was made at the same time that steps be taken to ensure that the Canton authorities (who were apparently intending to take separate action) should conform to any postponement of the enforcement of the regulations decided upon by the Nanking Government. It has now been ascertained that the enforcement of the regulations has been definitely postponed

until the 30th June, 1936, and therefore details of the objectionable features in the regulations are not included in this report. Action similar to that taken by the British Chamber was also taken by the General Chamber of Commerce at Shanghai, which has requested the diplomatic body to make appropriate representations to the Chinese Government.

- 310. In view of increasing pirating in China of British text books, the question of protecting for British copyrights has again been explored, and the matter informally discussed with the Chinese authorities. The position remains as before; British works produced in China, especially for the use of the Chinese people, could probably obtain protection under the Chinese Copyright Law; China has no inclination to join the Berne Convention or to conclude with His Majesty's Government a separate reciprocal treaty on acceptable terms. The Ministry of Industries has refused an application from a British firm for copyright protection for gramophone records: and His Majesty's Government declined to suggest that the Chinese Government should participate in a conference which the Italian Government proposed to convene in the autumn of 1935 to discuss questions relating to the protection of the gramophone record.
- Repeated but still unavailing representations have continued to be made by this Embassy regarding imitations of the "Hazeline Snow" trademark, owned by Burroughs, Wellcome and Co., and of the "Lux" and other trade-marks owned by the China Soap Company (Lever Brothers) (see annual report 1934, paragraph 219). Messrs, Burroughs and Wellcome's appeal to the Executive Yuan was disallowed on the 9th January, and no further action has been taken. Messrs. Lever Brothers appeal to the Ministry of Industries was informally supported by His Majesty's Ambassador's representative, who handed a copy personally to the Minister of Industries. A case in which the China Soap Company has brought repeated actions against an imitator in Soochow, named Li Yih-kee, of William Gossage and Sons' "Ziang Mow" mark, which have been appealed and sent back for retrial on more than one occasion between the local district court and the provincial court, may be regarded as an example of the difficulty of securing effective execution of judgment, and of the opportunities afforded by the law for procrastination; it is cited by the company as an example of the timidity, if not venality, of the Chinese courts. The cases appear, however, to have been badly presented by the company's legal representative. In connexion with this case another series of actions has arisen, in which the British company has sought to obtain, against the same defendant under the name China Ziang Mow Foreign Candle and Soap Factory, cancellation of the registration of a trade-mark including the two characters "Ziang Mow," which have involved highly technical legal interpretations of article 15 of the trade-mark law (now article 14 of the new law); application was made to the Trade-mark Bureau and refused, an application to the bureau for a "protest re-examination" was likewise unsuccessful, an appeal to the Ministry of Industries was unsuccessful, and a further appeal to the Executive Yuan having also failed, the company in August appealed to the administrative court and sought the intervention of this Embassy. His Majesty's Ambassador's representative at Nanking presented a memorandum of the facts to the Waichiaopu, and while disclaiming any intention of intervention while the case was sub judice, made oral representations at to the mala fides of the Chinese company, and suggested that in the plain meaning of artice 15 of the law the registration of the mark should be cancelled. On the 30th November the appeal was rejected by the administrative court, and the company sought the support of this Embassy in applying for a retrial. His Majesty's Ambassador's representative orally drew the attention of the Ministry for Foreign Affairs to the importance of the issues at stake and requested that the company's application receive the most careful consideration. The Vice-Minister for Foreign Affairs replied that the case would be dealt with in accordance with the law, and that he was unable to exercise any influence in the matter. In July the China Soap Company called attention to a decision of the Trade-Mark Bureau (in connexion with efforts made by the company to obtain registration in colour of the Vinolia Boracic and Cold Cream Soap Carton), that mere difference in size or shape in which a mark is employed is sufficient to invalidate a claim to prior use. The company desired no intervention in this case, which they were confident of settling by their own efforts; but His Majesty's Ambassador suggested

informally to the Chinese authorities that the exclusive right of trade-mark owners to use a registered mark in all shapes and sizes should be explicitly safeguarded in the new law.

- 312. It is against the Trade-Mark Law, and its interpretation by the courts and their inability to enforce judgments that complaints have been made. There has been no criticism of the operation of the Trade-Mark Bureau, which has, in fact, on at least one occasion to which the attention of this Embassy happens to have been drawn, gone out of its way to be helpful. With regard to the judiciary, a case was reported to this Embassy in January 1935 in which, after legal proceedings extending over four years, the administrative court, finally, and in favour of the British trade-mark owner, overruled a decision of the Executive Yuan. As regards both the operation of the bureau and the proceedings of the courts no complaints have been made during the year except on behalf of the Lever interests, whose policy appears to be to pursue the owners of offending marks with the utmost rigour to the utmost limits of the law.
- As stated in the section on legislation, the revision of the Trade-Mark Law, from which so much had been hoped, proved utterly disappointing, none of the defects to which British interests had drawn attention being remedied in the new law. The recommendations of the Trade-Mark Sub-Committee of the British Chamber of Commerce, as communicated informally through this Embassy to the Chinese authorities concerned, were briefly: (a) amendment of article I to ensure that registration of a mark without limitation of colour should give protection in all colours; (b) that the provisions of article 15 as to fraudulent use of trade names be extended to cover similar as well as identical names; (c) that article 27 be amended to give protection against imitation in categories other than those in which the mark is registered, if the owner can show that his interests are likely to be prejudiced or that the public is likely to be deceived; (d) that the sub-divisions in which marks may be registered be reduced; (e) that provision be made for the right to apply to the courts for injunctions; f) that a new provision be made in the law for the issue by the Trade-Mark Bureau of certificates of opinion (for use in legal proceedings). As stated above, the desirability of protecting marks in all shapes and sizes was also brought to the attention of the Chinese authorities by this Embassy.
- 314. The desirability of the conclusion of an agreement between His Majesty's Government in the United Kingdom and Japan which would give mutual protection in (Manchuria and) China to the nationals of the one against imitations of trade-marks by the nationals of the other has been brought to the attention of this Embassy by the British Chamber of Commerce at Shanghai, and is under consideration. Only one clear case of imitation in China by a Japanese of a British mark has been reported during the year, and that has, as usual, been dealt with administratively by the Japanese consular officer concerned.
- Japanese commercial activities during the year have been principally concentrated on the economic penetration of North China. In July, as part of his "three-point programme," Mr. Hirota is believed to have formulated for discussion with the Chinese Ambassador at Tokyo six proposals for Sino-Japanese economic co-operation, to be carried out from headquarters in Tientsin; these appear to have been the improvement of cotton cultivation and sheep raising for wool, and the general increase and improvement of North China agricultural products; the encouragement of certain industries, particularly the spinning of coarse cotton yarns and the manufacturing of cement; the exploitation of the mineral resources of the country, especially coal and iron; the extension of communications, especially from the coast inland, and as between Manchukuo and North China; the formation of some joint trade association to adjust mutual industrial, commercial and financial interests; and a readjustment of the Chinese import tariff to effect reduction of the very high duties on certain articles in the import of which into China Japan is principally interested. Plans were made for the establishment of a vast Japanese investment company, known as the Hsingchung (or Kochu) Company, in which the South Manchuria Railway were to be the principal partners, the object of the company being joint Sino-Japanese investment in North China; the company was eventually established in December at Dairen, and the South Manchuria Railway Company reorganised the administration of its business in China by establishing a head office in Tientsin, from

which its investigations with a view to finding profitable investments for the Hsingchung Company may be made. The capital of the new company is stated to be only 10 million yen; so far, neither Chinese nor Japanese capitalists appear to have evinced any desire to make large-scale investments. The Japanese view appears now to be that investments must await a more friendly attitude on the part of the Chinese, and Japanese endeavours have been mainly concentrated on securing their position in North China strategically and politically. Some progress in this direction has already been made, particularly in connexion with the improvement of communications. Free postal intercourse between North China and Manchukuo has been uninterrupted during the past year, and an agreement for a through telegraphic service was come to in the course of the summer, final agreements with regard to outstanding points being made in November. Through passenger traffic on the Peking-Mukden Railway has also been uninterrupted during the year. Negotiations for through freight on the Peking-Mukden Railway, and for an air service between Peking and Mukden, are being carried on, but have not yet reached a conclusion. It is not known whether negotiations for the extensions westwards of the Peking-Suiyuan Railway and the Shantung Railway, and for the construction of a new railway from Taku, through Tsang-chow, to Shihchiachuang have met with any success. No progress appears to have been made in connexion with improved production of cotton and wool, though it has repeatedly been stated that the basis of Sino-Japanese economic co-operation in North China must essentially be co-operation between an industrialised Japan and a China capable under Japanese supervision of producing the raw materials which Japan requires. Similarly, in the industrial sphere little, if any, actual investment by Japanese appears to have been made. With regard to mineral enterprises, the Japanese have displayed a lively interest in the affairs of the Kailan Mining Administration, and they have in fact secured control of the Shihmenchai coalfield, which lies immediately to the north of Chinwangtao. They have also, it is believed, actively participated, though to what extent is not known in financing anthracite coal mines at Mentoukou, and bituminous coal mines at Chaitang, some 40 miles west of Peking. There is also reason to suppose that negotiations have been in progress for Japanese investment in the Liuhokou mines in Northern Honan. As a result of a visit in the autumn to Japan by a Chinese economic mission from Shanghai, it was decided to establish in China a Sino-Japanese trade association, which should deal with commercial, industrial and other economic matters of mutual interest, but at the close of the year this project was still in abeyance, owing it is understood to the political situation in North China which the Japanese felt to be unsatisfactory. With regard to any readjustment of the Chinese import tariff, no progress had been made before the end of the year, but it is commonly supposed that the unrestricted smuggling in which Japanese and Koreans, who have been the principal offenders, have been allowed to indulge may be utilised as a pretext for demanding a reduction of import duties. In short, although little actual investment by Japanese appears so far to have been made, they have achieved a certain measure of success in establishing a strategic and political position in North China which would ensure that the economic penetration of the country might be safely undertaken.

- 316. An unofficial American trade mission, with an influential personnel under the leadership of the Hon. D. Cameron Forbes, reached China in April after visiting Japan and left on the 18th June after two months' investigation in all the principal centres of foreign trade. Elaborate preparations were made everywhere for their reception, which was most cordial. It was emphasised that the mission was merely a "fact-finding" body with no executive functions or political significance. Their attention is understood to have been directed mainly to transport and communications, tariff reciprocity, investment in Chinese industries, and the expansion generally of American trade with China. They were nowhere able to escape discussion of America's silver-buying policy.
- 317. No action on the part of this Embassy has been called for in connexion with the regulation of the import of eggs into the United Kingdom beyond transmitting to the Chinese Government a memorandum relating to restricted imports of eggs in shell in the second quarter of 1935.
- 318. The Chinese Government have reaffirmed that the combination of ad valorem and specific duties imposed on raw silk under the Indian Tariff

(Textile Protection) Amendment Act, 1934, has increased the duties 200 per cent. and has almost stopped the import of Chinese silk into India. In February the Chinese Ambassador in London suggested abolition of the specific duty, and the imposition of the ad valorem duty on Chinese silk on its actual value. The Indian Government repeated that the revised duties were protective and adjusted to meet the needs of the Indian sericultural industry, they added that they saw no reason to revise the tariff values in advance of the usual annual enquiry. It is to be noted, however, that at the end of 1934, as the result of representations made by Canton, the Indian Government had made a partial reduction of duties in favour of certain kinds of Chinese silk piece-goods.

- The following questions in connexion with the Burma-Yunnan frontier trade have engaged the attention of this Embassy during 1935: On the 3rd July a despatch was received from the Government of Burma transmitting a communication dated the 16th May from the Revenue Department to Burma Customs Commissions to the effect, inter alia, that on the 1st June, 1935, import duties would be levied on saccharine, cigars, &c., matches, silk and artificial silk, and cotton and silk-cotton piece-goods, and also on silver bullion and coin (other than Indian currency). Apart from the import duty on silver, which was imposed in 1932 (and modified in 1934), the general trade from Yunnan into Burma had hitherto been free from taxation; on the 27th February His Majesty's consul at Tengyueh had written (with the concurrence of the Burma authorities) and assured the local chamber of commerce (in connexion with their contribution to the Bhamo hospital) that the Burma Government had no intention to tax imports from Yunnan; the receipt on the 1st June by the chamber of a notification that these new duties were to be imposed on that date consequently caused considerable embarrassment. On the 19th August a despatch dated the 27th July was received by His Majesty's Ambassador from the Government of Burma transmitting a communication from the Government of India dated the 25th June to the effect that, owing to the Quetta earthquake, the imposition of the land customs line was postponed sine die: On the 21st August the Government of India informed His Majesty's Ambassador that Customs at Bhamo were making arrangements to bring the land customs régime into force, but that no duties had been collected, except on silver. So far as is known, the new duties are not yet in force.
- 320. On the 4th February, 1935, by agreement between His Majesty's Government in the United Kingdom and the Chinese Government, the Chansi (Sansi) trade route across the Burma-Yunnan frontier, which was opened by article 9 of the Burma Convention, 1894, was formally closed.
- With regard to the import of silver from Yunnan into Burma, the Government of India have decided that the existing prohibition on imports of silver coins (other than Indian currency) shall, when the general land customs régime comes into force, be replaced by an import duty; His Majesty's Ambassador has informed the Foreign Office that he concurs in the view that such action is not incongruous with article 11 of the Burma Convention, since the Chinese Government have themselves held in the past that "cash" in the treaties does not denote Chinese silver dollars, and since His Majesty's Govern-the Government of India also desire to notify five trade routes by which alone silver may be imported from Yunnan into Burma; His Majesty's Ambassador has, on the understanding that the routes in question are already regarded by the Chinese authorities as open to trade (which appears to be the case), agreed that it is unnecessary to obtain the prior concurrence of the Chinese Government and His Majesty's Government, though some of the routes are not named in the Burma Convention and have never been formally opened by agreement. whole question is complicated by the facts that the export of silver from China is, in theory, prohibited (a prohibition in which His Majesty's Government has acquiesced) and that, nevertheless, the export of silver to Burma from Yunnan is an essential feature of the trans-frontier trade.
- 322. In view of the fact that import of alcoholic beverages from Burma into Yunnan is prohibited by article 11 of the Burma Convention, 1894, the Burma Government has hitherto abstained from granting a refund on re-export to Yunnan of duty paid on spiritous liquors on import into Burma; His Majesty's

Ambassador has expressed the view that the retention of this prohibition is anomalous and that there is no objection to an informal approach to the Chinese Government for an agreement to regard it as null and void.

- 323. Cases in which embarrassment has been caused to His Majesty's consular officers and to this Embassy by the activities of, or by requests for support from, British companies in China which are not entitled to British protection, or from which British protection has been withdrawn, have occurred with increasing frequency. As a result, the whole question has once more been reconsidered and outline proposals for new legislation to obviate the continued existence of such companies in China have been drawn up and submitted to the Foreign Office. Two cases, in particular, which have given rise to much difficulty and correspondence, have been the liquidation of the National Commercial and Savings Bank (Limited) and the fraudulent sale of lottery bonds by the Associated Investments (Limited). A decision by a Chinese court at Hankow to assume jurisdiction over Centrosojus (England) (Limited) was the subject of a protest by His Majesty's consul-general; the case was, however, eventually settled out of court.
- 324. By the (Hong Kong) Companies Amendment Ordinance, 1935, British firms are no longer required in their Chinese names to state their British nationality (see annual report 1934, paragraph 218).
- 325. The questions of the export of munitions from the United Kingdom to China, of munitions in transit through, or exported from, Hong Kong (and Singapore) to China, and of the support to be accorded to representatives of British munition suppliers, are dealt with in the United Kingdom section of this report.

IX.—CUSTOMS AND TARIFFS.

- 326. The question of the reappointment of Mr. Kishimoto as chief secretary, which is principally of interest in connexion with possible Japanese demands that on Sir Frederic Maze's retirement a Japanese shall be appointed to the post of Inspector-General, has been settled temporarily at least (see paragraphs 232 to 234 of the annual report 1934). On his return in January from leave the Inspector-General was consulted by the Minister of Finance as to the predicament in which the Chinese Government found itself as a result of having appointed Mr. Kishimoto as Commissioner of Customs at Tientsin, and having confirmed Mr. Ting's appointment as chief secretary. It was clear that the Japanese would in the end either demand Mr. Kishimoto's reappointment as chief secretary or his appointment outright as Deputy Inspector-General. Sir Frederic Maze discussed the matter with the Japanese Ambassador, and an agreement was reached by an exchange of letters on the 16th January, in accordance with which Mr. Kishimoto was reappointed for the time being to the post of Chief Secretary on the understanding that the appointment was, like other appointments of inspectorate secretaries or port commissioners, not of a permanent nature, appointees being liable to removal or transfer.
- In connexion with the discussions relating to proposals for an international sterling loan to China for purposes of currency reform, His Majesty's Ambassador and Sir Frederick Leith-Ross on the 29th October made it clear to the Japanese Ambassador that British participation in such a loan would depend in part on an assurance that the present system of customs administration under a British Inspector-General would be maintained, and that the recruitment of foreign personnel for the customs service would be resumed: the Japanese Ambassador, speaking personally, said he felt sure that his Government were quite prepared to see the Inspectorate-General remain in British hands, but he stated that the number of Japanese officials in the customs service was now disproportionately small, and he suggested that the formerly existing post of Deputy Inspector-General might be revived and a Japanese appointed to it. His Majesty's Ambassador stated that, so far as he was aware, His Majesty's Government in the United Kingdom would be unlikely to have any objection to this course, subject to the understanding that the post of Deputy Inspector-General did not carry with it a reversion to the Inspectorate-General itself. In this connexion confidential information has been received from the Inspector-General that he has

put before the Chinese authorities the advantages of resuming recruitment of foreign employees in the customs on a permanent basis. As regards the nationality of the next Inspector-General, Sir Frederic Maze's attention has been drawn informally to the fact that the trade of the British Empire (as distinct from Great Britain) with China is greater than that of any other Power, and action has also been taken to make this clear in the acting commercial counsellor's recently published report on economic conditions in China.

328. In January 1935 it was known that the Tariff Commission was engaged on a revision of the import tariff, and throughout the year there have been persistent rumours that a new protective and revenue increasing import tariff (or a surtax on the present import tariff), and a drastically reduced export tariff accompanied by abolition of interport duties, were to be imposed (see annual report 1934, paragraphs 239 to 244). In April the Japanese consul-general at Nanking informed His Majesty's Minister that the Japanese Minister had strongly protested against a proposal to impose a general 10 per cent. surtax on all items of the import tariff. By the end of the year none of the measures proposed had been put into force, though it is noteworthy that the national budget for 1935–36, which was published at the end of June, made no provision for export and interport duties and included a new item for surtax; and that various loans have been stated to be secured on "the new increased tariff."

329. The collection of the 5 per cent. revenue surtax (see paragraph 236 of the annual report 1934) was on the 17th June, 1935, continued until the 30th June, 1936.

330. An exchange of notes attached to the Convention Sino-Indo-Chinoise, which was ratified in May 1935, by which certain goods imported from French Indo-China into the provinces of Yunnan, Kwangsi and Kwangtung are accorded special reduced rates of import duty, embody a principle of regional differentiation of tariff which appears contrary to (the spirit at least of) the declaration made at the Washington Conference as to the uniformity in the rates of customs duties at all land and maritime frontiers of China, and also in annex 4 of the Sino-British Tariff Treaty of 1928, and which is inherent with dangerous possibilities, since presumably similar arrangements might quite well be made, for instance, to goods imported from Manchukuo into North China. Representations to the Chinese Government are now under consideration.

331. Smuggling has reached proportions unprecedented since the days of the *lorcha*, and an extent which has not only threatened to bring legitimate trade in certain areas to a standstill, but has also seriously affected customs revenue. The contraband trade, in the export of silver, and in the import of almost all high duty-paying goods, has been principally carried on, in the Tientsin area and also in Shantung by Japanese and Korea Japanese subjects, in Fukien by Japanese Formosan subjects, and in Kwangtung by the provincial authorities.

332. The effects on British trade in Kwangtung are referred to in paragraphs of the trade section of this report relating to sugar and artificial fertilisers

333. In Fukien, while smuggling appears to be general and not confined to any particular class of goods, British interests have been principally affected by clandestine imports of lubricating and other heavy mineral oils.

334. The situation in Shantung is obscure, but it is understood that one of the principal articles brought in by smugglers is cigarette paper from Japan (see the paragraphs in the trade section of this report relating to the hand rolled tobacco industry).

335. In North China smuggling of goods across the Great Wall from Manchukuo has been continuous and considerable, but contraband principally enters this area from craft of all kinds, coming, it is understood, chiefly from Dairen, which run their cargoes on to the coast in the neighbourhood of Shanhaikwan, Chinwangtao and Peitaiho, and take them thence inland for transport by the Peking-Mukden Railway to Tientsin. The violence with which the Japanese authorities have prevented any interference with Japanese or

Koreans by Chinese preventive officers, and the withdrawal, under Japanese pressure, of the customs patrol boats, combined with the inability of the railway authorities to render effective assistance, have left this district entirely free to the operations of the smugglers; not only has legitimate trade in this area in many articles, as for instance sugar, been brought to a standstill, but Tientsin has become a general port of entry for contraband for the whole of North China, and there are indications that trade in Shanghai (for instance in artificial silk) has been even more seriously affected than it is in Tientsin itself. In a recent discussion of the problem by the consular body in Tientsin the Japanese consulgeneral explained that smuggling in China by the Japanese was not an offence under Japanese law. Nevertheless, the fact remains that when the Japanese authorities in the autumn of 1935 wished to prevent the clandestine export of silver by Japanese and Koreans they did so effectively and immediately by administrative action. On the 13th November the senior Ambassador circulated to his colleagues a letter from the consular body in Tientsin, urging that steps should be taken to prevent a continuance of contraband trade in this area: the majority of the foreign representatives were in favour of a joint representation to the Chinese Government, the Japanese Ambassador, however, expressed the view that it was a matter which principally concerned the Chinese authorities themselves, and that any representations by members of the diplomatic corps should be made individually.

336. There appear to be some grounds to suspect that the Japanese have abstained from measures to prevent smuggling by their nationals, because they contemplate the possibility of using the situation which has arisen as an argument for a downward revision of the Chinese import tariff, asserting that smuggling arises inevitably from the high duties now in force.

Prosecutions of British Subjects in Smuggling Cases.

337. In connexion with the prosecution by the Chinese Maritime Customs of certain British subjects in Shanghai on a charge of importing goods into China with the intention of evading customs duties, it was held by the magistrate that the provision regarding the burden of proof contained in Section 259 of the Customs Consolidation Act, 1876, did not apply to China. Correspondence ensued with the Foreign Office, with a view to bringing the law of evidence in customs cases in China into line with that in force in the United Kingdom.

Customs Preventive Ordinance.

- 338. In accordance with instructions from the Foreign Office, the informal general reservation of our treaty position which had already been made (see annual report for 1934, paragraph 250) was followed up in May by a formal reservation of any rights, secured either by treaty or by the Joint Investigation Rules of 1868, which might prove to be infringed by the operation of the Customs Preventive Ordinance or the revised Manifest Regulations.
- 339. As a result of confidential discussions with British shipping firms, the conclusion was reached in January that the adoption of a system of consular clearances coupled with naval protection, cannot be regarded, except in special circumstances, as a practical means to prevent encroachments by the Chinese authorities on the treaty rights of British shipping.

Arrest of Chinese Smugglers on British Ships.

340. The imposition of restrictions on the export of silver led to extensive smuggling, and brought up the question of the procedure to be adopted by the Customs when Chinese were found on a British ship with smuggled silver just before the vessel's departure. It seemed undesirable that the Chinese should be permitted to remove passengers or members of the crew from the vessel without production of a Chinese court warrant duly countersigned by the British court or consul, while to insist on the production of a warrant might cause serious delay to the ship. After discussion with the customs it was decided that it was unsafe to waive the legal requirements, but that there was no objection to the Customs obtaining blank sealed warrants from the court in advance, provided the consul's endorsement was obtained either before or after arrest. Consuls were circularised accordingly.

- 341. In January 1935 a British subject was prosecuted by the customs in His Majesty's provincial court at Canton for smuggling contrary to article 74 of the Order-in-Council, 1925, and was convicted of smuggling one case of whisky. He was fined £10 and the case of whisky was ordered to be confiscated. The Foreign Office approved a direction by the court that the confiscated goods be handed to the customs.
- 342. On the 31st December, 1934, the Minister for Foreign Affairs stated that the enforcement of the regulations governing the duty-free import of supplies for foreign military and naval forces (see annual report 1934, paragraph 247), had been postponed *sine die*.
- 343. On the 9th December, 1935, the British military authorities at Shanghai were refused clearance by the customs of 182 bags of flour, on the grounds that the application to import did not bear the stamp of the Internal Revenue Administration (which functions in the same building and which controls the various consolidated taxes, including that on flour). The brigadecontrols the various consolidated taxes, including that on flour). The brigade-major interviewed the head of the Administration, who said his instructions from the Minister of Finance did not cover military stores, but who signed the application on the understanding that a written request to that effect would subsequently be made. On the advice of His Majesty's consul-general, however, who felt we should avoid being manœuvred into the position of having to go to the Internal Revenue Administration to obtain their stamp on import applications, a letter was eventually sent merely stating that the application covered military stores, and asking that there should be no interference in future by the Internal Revenue Administration with such consignments. His Majesty's consul-general, however, informally warned the Commissioner of Customs of the possibility that the British military authorities might take their stores away out of hand. The Commissioner replied that, while he would do what he could, he would be compelled to refuse to pass import applications covering flour until stamped by the Internal Revenue Administration. His Majesty's Ambassador, subject to the proviso that all proper steps had been taken and that there was no possibility of arranging the matter with the customs, approved a proposal made by His Majesty's consul-general, should difficulties arise with the Internal Revenue Administration over the next consignment, to inform the British military commander that he had no objection to his sending men to fetch any stores the customs refused to pass. (With regard to the collection by the customs in respect of imports of the consolidated taxes, see the paragraphs relating to the consolidated tax system and to the new consolidated tax on alcohol in the taxation section of this report.)

X.—Conservancy and Other Works secured on Customs Surtaxes.

- 344. The provisional report and proposals drawn up by the Netherlands Harbour Works Company for the improvement of Chefoo Harbour were condemned by a representative of the Ministry of Railways (see paragraph 261 of annual report, 1934), who recommended a modification which was in turn condemned by the customs engineer-in-chief. The Commissioner of Customs then drew up a compromise plan which was submitted by the commission to the Chinese Government in January 1935. At a meeting of the commission on the 29th October, the new Chinese chairman reported that there was no prospect of the Government providing any financial assistance, and the commission thereupon decided to proceed with the dredging of the harbour and subsequently with such other necessary works as the funds at its disposal would permit. In reply to protests from the Netherlands Harbour Works Company that the call for tenders for the dredging work would infringe their rights under the alleged contract of 1933, the commission stated that, while not admitting the alleged contract, they would be interested to receive a tender from the company for the dredging, and would give the company special consideration.
- 345. The Netherlands Minister proposed that the attention of the Ministry of Finance be drawn to a statement he had made in December 1933, to the then Netherlands Minister, that "the Chinese Government intends to leave the sum of 500,000 dollars to the credit of the Chefoo Harbour Improvement Commission, and

the Government undertakes, as the work on the Port of Chefoo proceeds, gradually to place the necessary funds at the disposal of the commission." His Majesty's Ambassador concurred, but suggested that such representations be made individually, and added that he was instructing his representative at Nanking to explain informally that dredging of the harbour was urgently necessary, and should be proceeded with by the commission without waiting for a decision regarding the proposals submitted in January 1935, unless the Government could immediately provide the funds necessary to carry out those proposals. The American Ambassador took similar action. The Japanese Ambassador, while concurring in the suggestion made by the Netherlands Minister, and instructing his representative at Nanking to take appropriate measures, expressed the opinion (which has passed without comment) that "regarding the more important matters of the harbour improvement works, the Chefoo Harbour Improvement Commission should be duly supervised by the Diplomatic Body."

- 346. In February informal representations were made by His Majesty's Minister's representative at Nanking to the effect that, as sufficient funds had been collected for the construction of the Hsiho bridge, the levy of the International Bridge Surtax (at Tientsin) should cease. Similar representations were made by the other interested Powers, and identic replies were eventually received from the Waichiaopu on the 21st September stating that in addition to the Hsiho bridge it was essential to reconstruct the ex-Austrian bridge and to construct a new bridge to connect the first and third special areas, and expressing the hope that the foreign representatives and foreign merchants would concur in the continuance of this surtax.
- 347. With regard to the divergence of view which exists amongst the foreign representatives as to the rights conferred on the Chinese Government by the tariff autonomy treaties to levy local ad hoc taxation in the form of surtaxes on customs duties (see paragraph 259 of annual report, 1934), the Foreign Office decided that the circumstances in this case called for no modification of the attitude we have adopted since 1929 towards such local taxation for conservancy purposes.
- 348. In March 1935 the Waichiaopu sent an identic aide-mémoire to all the foreign representatives stating that the Haiho Conservancy Commission had been transferred to the jurisdiction of the National Economic Council and that the vacant post of engineer-in-chief was to be filled by an official selected by the council. As the commission had already, in accordance with the usual practice, selected a successor and had in October 1934 approved the appointment of Mr. Muller, who had already assumed his duties, they were placed in an embarrassing position. Informal representations were made by the British and American representatives, pointing out the facts of the case, and expressing the opinion that the matter of filling the vacant post should properly be left in the hands of the Haiho Conservancy Board. The French Minister made a formal protest against the measures referred to in the Waichiaopu aide-mémoire, on the grounds that such action would be contrary to the provisions of the Peking protocol from which the commission was derived. As the result of repeated informal representations instructions were issued by the Ministry of Finance to the Superintendent of Customs at Tientsin, whose signature as a member of the commission was necessary for the validity of Mr. Muller's contract, and the latter's appointment as chief conservancy engineer was eventually signed and completed on the 12th December, 1935, the appointment to date as from the 20th January, 1935, when he took charge of the commission's engineering department.
- 349. This question appears to have been satisfactorily settled, and no other difficulty has yet arisen in connexion with the functioning of the National Conservancy Board (see paragraph 263 of annual report, 1934).
- 350. Work on the conservancy of the Whangpoo, and on the Min River, has progressed satisfactorily, and no questions have arisen regarding these surtaxes. A new dredger for work on the Fairy Flats, the contract for which went by open tender to a German firm, has given satisfactory performance and a second may shortly be ordered.

351. In December the Kunglingtan Conservancy Commission was reorganised as the Upper Yangtze Conservancy Board, consisting of seven members, of whom one is the Commissioner of Customs and one a foreigner, under the chairmanship of the Superintendent of Customs. The functions of the board, which will operate in close connexion with the Customs and not under the Szechuan Navigation Bureau, will be to improve the navigation of the Yangtze between Ichang and Chungking. It is proposed and unanimously agreed by the foreign commercial interests that the board shall levy the conservancy tax levied during 1931 to 1933 by the former commission. The Japanese consul has refused to concur and has referred the matter to his Government.

XI.—BOXER INDEMNITY.

- 352. In May Mr. N. S. Brown resigned from the board of trustees in China, and Mr. H. V. Wilkinson, of Mackinnon Mackenzie and Co., was appointed to the board, the foreign members of which now include, in addition, Mr. J. B. Tayler, Mr. R. Calder Marshall and Mr. W. S. King.
- 353. In November the name of Mr. Arthur R. Guinness, a partner of the banking firm of Guinness, Mahon and Co. and a director of several financial trusts, was submitted to the Chinese Government by His Majesty's Government in the United Kingdom as successor on the Chinese Government Boxer Indemnity Purchasing Commission to Sir Basil Blackett, who was killed in a motor car accident.
- 354. In August the third group of Chinese students, numbering twenty-six, to be sent to study in England with scholarships granted by the board of trustees in China for the British indemnity funds sailed for England (see paragraph 265 of the annual report for 1934) and have all been placed in different universities in the United Kingdom. There are now thirty-five of these scholarship holders in the United Kingdom.

XII.—AVIATION.

- 355. During the period under review considerable progress has been made in both civil and military aviation. Funds for the purchase of aeroplanes have been obtained from the National State Lotteries and from private and public subscriptons.
- 356. Considerable expenditure has been incurred in the establishment and development of the large and up-to-date military air stations at Hangchow, Loyang and Nanchang, and the Central Government can now boast of having a modern air force, consisting of approximately 200 first-line aircraft and 150 training machines.
- 357. There has been an increase of traffic on the commercial air services, and new air routes have been established.

Sales of Aircraft.

- 358. The Commission on Aeronautical Affairs has purchased 120 military aircraft, of which 45 are of Italian and 10 of French manufacture. The remainder were imported from the United States.
- 359. In addition to the above, 56 aeroplanes have been constructed in the Curtiss Wright factory at Hangchow, the engines and components being obtained from America.
- 360. The air force authorities appear to be far from satisfied with the Italian aircraft which have been purchased, and it is probable that the majority of future orders will be for American craft.
- 361. It is disappointing to record that only one British aircraft, an autogiro, has been sold to the Central Government. Representatives of British aviation interests in China attribute their lack of business principally to the indisposition of the British aircraft manufacturers to be stirred from their contented apathy towards China and their preoccupation with assured markets at home and elsewhere.

Provincial Air Forces.

362. Although some Provincial Governments still retain a few aircraft, with the exception of those in Kwangtung, and possibly Kwangsi, their numbers and fighting value are unworthy of serious consideration.

Kwangtung.

363. The Kwangtung air force consists of six service squadrons equipped with a heterogeneous collection of approximately sixty aircraft, the majority of which are of obsolete types. Ten new Boeing Type P.E. 126 single-seater fighters, however, are now on order. There are also approximately thirty training aircraft.

Kwangsi.

- 364. The Kwangsi air force consists of one service squadron equipped with approximately twenty aircraft of various types, including Westland Wapiti and Avro 637. There are also forty training aircraft. Nine Nakajima Type 91 and nine old Nieuport single-seater fighters have recently been purchased from Japan.
- 365. Owing to lack of business, a vigorous retrenchment policy has been forced upon the Far East Aviation Company, and Captain Very Harvey, general manager in Hong Kong, and Flight-Lieutenant A. D. Bennett, the manager of Aircraft China (Limited), Shanghai, have both resigned and returned to England.

Far East Flying Training School, Hong Kong.

366. The Far East Flying Training School has managed to maintain its position, although the number of students has decreased. Nineteen members of the Hong Kong Volunteer Air Arm and three Chinese are now being trained as pilots, and nineteen Chinese are taking the ground engineering course.

Foreign Air Missions in China.

- 367. The three-year contract with the United States aviation mission, which expired in May 1935, has not been renewed, and Colonel Jouett and his staff have resigned (see paragraph 278 of last year's report).
- 368. The Italian air mission appears to have lost favour, and General Lordi returned to Italy in August on a plea of ill-health. He has been succeeded by General Silvio Scaroni, who was formerly Italian air attaché in London and Washington.

Aircraft Factories.

- 369. The output from the Curtiss Wright aircraft factory at Hangchow (see paragraph 277 of last year's report) was fifty-six airframes, and cost accounting reveals the fact that local construction effects considerable saving as compared with the price of imported aircraft.
- 370. Work on the Curtiss Wright factory in Kwangtung has been considerably delayed, but it is anticipated that the factory, when completed, will be capable of supplying the requirements of the provincial air force, except for engines which will continue to be imported from abroad.
- 371. It is reported that, in spite of opposition from the Italian air mission, the contract for a Sino-German factory has been concluded.
 - 372. The Sino-Italian factory at Nanchang is now under construction.

Air Communication.

373. Aircraft have been used extensively as a rapid means of communication by General and Mme. Chiang Kai-shek, General Chang Hsueh-liang and other important Government officials. A small fleet of air transports is used for this purpose. The facility and rapidity with which General Chiang Kai-shek and his staff can cover enormous distances by air have undoubtedly contributed very largely to his success and the expansion of his sphere of influence.

Civil Aviation.

China National Aviation Corporation.

374. The results achieved by this company have been satisfactory. New equipment, including two Douglas D.C. 2 and three Ford air liners, have been purchased and passenger fares have been reduced. There have been no serious accidents. Passenger traffic shows an increase of 130 per cent. as compared with 1934, and many of the services have been accelerated.

375. A twice-weekly air service between Chungking and Kunming (Yunnanfu) was inaugurated on the 1st April. Survey flights between Canton and Hanoi have been carried out with the object of establishing a regular service to connect at Hanoi with '' Air France.''

376. The increase in traffic and mileage flown is shown in the following table:—

Year.	Kilometres flown.	Passenger Kilometres flown.	Passengers carried.	Kilogrammes of Mail carried	
1935 (10 months)	1,435,460	2,553,283	5,224	58,052	
	1,594,088	4,389,555	7,932	55,310	
	1,890,000	5,875,000	10,400	64,000	

Eurasia Aviation Corporation.

377. The financial position of this company is still unsatisfactory, but the capital has been increased by 2,400,000 dollars, and three new 18-seater Junkers air liners have been purchased.

378. Owing to lack of traffic the Peiping-Hankow-Canton service was suspended in July, but a twice-weekly service between Sian and Chengtu was established in September.

379. There have been three serious accidents, in which two German pilots and one wireless operator were fatally injured.

South-Western Aviation Corporation.

380. Owing to lack of capital, the only services which are in operation are those between Canton and Lungchow and between Canton, Kiungchow (Hainan Island) and Nanning.

Survey Flights, Penang-Hong Kong (via Saigon and Tourane).

381. A series of test flights, the first of which was made on the 2nd October, are being carried out by Imperial Airways between Penang and Hong Kong, and the establishment of a regular air mail service is anticipated.

XIII.—LEGISLATION.

382. Yet another draft Permanent Constitution of the Republic of China was produced in October, and this has now been adopted by the 5th National Congress of Kuomintang delegates, held in the middle of November, and referred to the incoming Central Executive Committee for further revision before formal publication and submission to the National People's Congress in October 1936.

383. The most important pieces of legislation enacted by the National Government during the year under review were the revised Criminal Code, and the Criminal and Civil Codes of Procedure. These came into force simultaneously on the 1st July, 1935.

384. Other legislation of importance affecting British subjects which was issued during 1935 comprised a Bankruptcy Law (promulgated the 18th July, enforced the 1st October), a revised Trade-Mark Law (Promulgated and enforced the 23rd November), an Insurance Enterprise Law (promulgated the 5th July),

and a Law for the Enforcement of the Land Law (promulgated the 5th April). Of these the two last enactments are not yet in force. A Stamp Tax Law, promulgated the 8th December, 1934, and a Co-operative Enterprises Law, promulgated the 1st March, 1934, both came into force on the 1st September, 1935.

385. In the case of the Bankruptcy Law an expression of opinion was sought by the Chinese authorities from the foreign as well as Chinese interests likely to be affected, but the law, as finally enacted, differed little from the original draft submitted for the consideration of the foreign interests in question. Representations were made to the Chinese Government on the subject of the Insurance Enterprise Law, certain provisions of which, apparently intended to apply to foreign companies, would if enforced against British subjects have infringed our treaty rights, and a memorandum of the objections of the British insurance companies to the law, in so far as their interests were affected, was also communicated to the Chinese Government. As regards the Trade-Mark Law, the revision made did not include the amendments as suggested by the British Chamber of Commerce, which were communicated to the Chinese authorities concerned. The effect of the Co-operative Enterprises Law on British interests, especially the Asiatic Petroleum Company in Kiangsi, is discussed in another part of this report.

386. Among minor legislation may be cited regulations governing flights of foreign aircraft over Chinese territory, revised enforcement rules for the film censorship law, a law governing summonses and trials (the so-called "Chinese Habeas Corpus Act"), an ordinance governing marine radio stations, i.e., wireless on steamers, and two further sets of measures issued by Chiang Kai-shek as chairman of the Military Affairs Commission, providing for the progressive suppression of opium and narcotics. Ordinances were also promulgated in November governing privately-operated railways, railways operated by provincial and local governments, and railways used for special purposes (as by coal-mining concerns). Enforcement Rules for the Game Law were issued on the 25th October, and these and the Game Law itself come into force on the 1st January. 1936. A revised ordinance governing chartered accountants was promulgated, and came into force on the 4th May, and an Audit Law (Law of Accounting) was promulgated on the 14th August, but still awaits a mandate fixing the date of enforcement.

387. A mass of minor legislation was also issued dealing with military matters, and with examinations for the civil service, and with public officials in general. Of these the only items which need be mentioned are the Garrison Ordinance, Draft Provisional Rules for a National Military Service Register, and an Ordinance governing a Code of Military Etiquette in the former category, and an Examinations Law in the latter category.

XIV.—PROPAGANDA.

388. In the course of the present year it was announced that a total of 504,000 dollars was expended by the Chinese Government on propaganda during the year 1934.

389. Official news and national propaganda continue to be disseminated, as in the past two years, through the medium of the press, the cinema and the radio. It has been ascertained that a "Ministry for Foreign Affairs Special Fund" exists, amounting at the most to about 30,000 dollars a month, which is distributed amongst various news agencies, newspapers and individuals in China.

390. In Shanghai there are being used for the purpose of propaganda some seven daily newspapers in the Chinese language, with an approximate circulation of 42,000, one daily newspaper in the English language, three periodical newspapers in the Chinese language, four periodical newspapers in the English language and five news agencies. These organs are subsidised directly or indirectly by the Central or Provincial Governments. In Canton His Majesty's consul-general states that Government subsidies to private newspapers have been reduced to insignificant figures, and that a very effective censorship has been maintained over the press. It is understood that 3,000 dollars has been put aside for subsidies to Chinese newspapers in Hong Kong.

- 391. There are some forty-four radio stations in Shanghai, six of which are frequently used for broadcasting Kuomintang propaganda. During the year a new station has been constructed which will be placed under the direction of the Bureau of Public Utilities for the purpose of broadcasting news in accordance with the instructions of the local Chinese municipal authorities. Programmes will be prepared by a special committee consisting of representatives of various organs of the Shanghai City Government and educational bodies in Shanghai. All municipal, middle and primary schools are being required to purchase receiving sets so that they may listen in to the educational parts of the programmes.
- 392. The only development of note during the year with regard to propaganda by means of the cinema was the establishment at Nanking in July, under the auspices of the Propaganda Committee of the Central Kuomintang, of a Central Cinema Studio. The studio is under the direction of a Mr. Chang Chung and produces "news reels" and films depicting modern factory conditions. Two of these films have so far been shown locally and at Shanghai with moderate success. The system of censoring films remains the same as in 1934 (see paragraph 302 of the annual report for 1934). With a view to encouraging the production of Chinese films, however, foreign films are required to pay a censorship fee of 20 dollars per 500 metres, whereas Chinese films are exempted. Furthermore, all Chinese films must be in the "mandarin" dialect, the use of which, it is considered, tends to unify the country, while the use of provincial dialects would have the opposite effect.
- 393. Budget estimates for financial aid to cultural institutions and schools in the outlying territories during the twenty-fourth fiscal year, passed by the Mongolian and Tibetan Affairs Committee in Nanking in February, exceed grants for the twenty-third fiscal year by 20,000 dollars. A grant of 5,000 dollars has been sanctioned by the National Government to the National Amateur Athletic Association.
- 394. There has been no outburst of anti-British or anti-foreign propaganda in the course of the year, an attempt at open anti-Japanese propaganda at Hankow having been quickly suppressed following the intervention of the Japanese consul-general.

XV.—CLAIMS.

- 395. In March as a result of the instructions received from the Foreign Office in November 1934 (see paragraph 308 of annual report for 1934), a memorandum was presented to the Waichiaopu suggesting that as a first step to the checking and settlement of the accumulated claims of British subjects against the Chinese Government, agreement should be reached between His Majesty's Government in the United Kingdom and the Chinese Government on the general principles by reference to which the admissibility of such claims was to be judged, which, in the opinion of His Majesty's Government ought to be in accordance with the well-accepted principles of international law. The memorandum further suggested that the work of assessment should be carried out by a Sino-British Joint Commission. The Chinese Government were urged to give early and careful consideration to these proposals, but by the end of the year no reply to the memorandum had been received. In an interview with His Majesty's Ambassador at the end of March, however, the Vice-Minister for Foreign Affairs expressed the opinion that the time was inopportune to raise the matter, and also made several other objections to the proposals of His Majesty's Embassy. The United States Embassy have been kept fully informed of the action taken by His Majesty's Embassy in this matter. Representations by the United States Embassy to the Waichiaopu on similar lines have met with no greater success.
- 396. The Chinese Government refused to agree to the offer of His Majesty's Government to accept £6,218 5s. $1\frac{1}{4}d$. in settlement of the amount of 110,640·47 dollars claimed by His Majesty's Government to be outstanding in respect of the Nanking claims, but offered to pay £1,571 5s. $5\frac{3}{4}d$. As it appeared after consideration that the Chinese Government could not be held entirely responsible for the discrepancy in the calculations of the sum payable, and that His Majesty's Government would be unlikely to succeed in obtaining either by

arbitration or by further representations any sum in excess of the amount offered by the Chinese Government, His Majesty's Ambassador under instructions accepted the offer of the Chinese Government on the 11th June. A draft for the amount in question was sent to His Majesty's Embassy by the Waichiaopu on the 30th December.

397. A number of other claims and debts were settled in the course of the year.

398. The monthly instalments under the agreement for the repayment of £16,605 0s. 9d. between the Ministry of Communications and three British firms signed last year (see paragraph 310 of annual report for last year) have been regularly paid.

399. At the end of January His Majesty's Embassy was informed that the Chinese Government were prepared to make an ex gratia payment of 8,000 dollars (the Government of India had claimed 9,000 rupees) in respect of the losses sustained as a result of the attack on the British consulate-general at Kashgar on the 14th February, 1934. His Majesty's Ambassador was instructed to accept this offer on the understanding that it could not be accepted as a final settlement for all losses in the recent disorders in Sinkiang, but only for losses arising directly out of the attack on the consulate-general. The Chinese Government effected payment of the sum agreed to in May. Lists of further claims for losses incurred in the Sinkiang disorders are being prepared by His Majesty's consulgeneral at Kashgar, and will be presented to the Chinese Government when received.

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400. In April His Majesty's consul-general at Shanghai reported that the solatium offered by the Japanese Government to certain British subjects for the losses suffered by them during the Sino-Japanese hostilities at Shanghai in 1932 (see paragraph 311 of report for last year) had been full paid. Moreover, the Japanese Government paid in addition 6,000 yen to Commander Davies, who was left destitute as a result of the destruction of the Woosung Forts Hotel at that time, although Japanese responsibility for this act has never been established. It is believed that the generosity of the Japanese Government on this occasion was due to past services rendered to them by Commander Davies during the Sino-Japanese war of 1894. The Chinese Government have refused to pay Commander Davies any compensation, although he put in a claim for 24,575 dollars.

Minute Paper.

Register No.

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SECRET.

POLITICAL DEPARTMENT

Dated

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	Date.	Initials.	SUBJECT.
Under Secretary Secretary of State Committee Under Secretary Secretary of State		D3	CHINA. Annual Report, 1934.

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FOR INFORMATION.

The following passages are of direct interest to India, and are useful summaries of events which they cover:-

Page 9 Sinkiang

Page 11 Tibet

Page 20 Burma-Yunnan Frontier.

Other passages in the Report which are of more general interest are sidelined in pencil, in particular:-

Mongolia (page 8) Communism (page 13) Sino-Japanese Relations (page 23) Financial situation (page 41) The Chinese Tariff (page 51).

Previous papers 4483

POLITICAL COMMITTEE

& O. Secretary & J. (S) Secretary.

For information.

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1935

CHINA.

Annual Report, 1934.

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Sir A. Cadogan to Sir John Simon.—(Received March 5.)

(No. 1.)

Sir,

Peking, January 1, 1935.

I HAVE the honour to transmit herewith the annual report on China for

I HAVE the honour to transmit herewith the annual report on China for the year 1934. I am indebted for the preparation of this report to the members of my staff, who have all contributed their respective sections and generally assisted in its compilation.

2. In accordance with the instructions contained in your despatch No. 49 of the 23rd January last, His Majesty's consul-general at Mukden has been entrusted with the writing of an annual report on Manchuria and the Kwantung Leased Territory. No separate section on Manchuria, therefore, is included in the enclosed report.

I have, &c. ALEXANDER CADOGAN.

Enclosure.

Annual Report on China for 1934.

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I.—INTERNAL POLITICAL SITUATION.

(1) General.

THE year 1934 in China has been one of marking time, with events waiting on developments in the relations between China and Japan. These have, as in the preceding three years, dominated the internal situation and necessarily form the background of any review of political developments and the progress of the Chinese Government during the year.

- 2. The character and composition of the Chinese Government have remained generally the same as they were in 1933, that is to say the Administration has remained under the nominal direction of Wang Ching-wei (as head of the Executive Yuan and concurrently Minister for Foreign Affairs) and his colleagues, while the real power has been exercised in the background by Chiang Kai-shek from his post as Chief of the Military Affairs Commission and de facto generalissimo of the armed forces of the Central Government.
- It will be recalled that the preceding year 1933, had seen the extension of the direct control of the National Government into North China and a general strengthening and consolidation of their influence in all parts of the country excepting the south-west. In November, however, the political outlook had suddenly been clouded over by the outbreak of the rebellion of the XIXth Route Army and the establishment of the Separatist Government of Chen Ming-shu and Eugene Chen in Fukien. The year 1934 thus opened in an atmosphere of anxiety and suspense; and the independent Fukien Government had been in existence for some weeks before Chiang Kai-shek, having completed his preparations and placed the Government forces in position, struck in the early days of the new year. In the result the rebel movement collapsed as suddenly as it had arisen. The forces of the National Government, advancing into Fukien from the Chekiang border and assisted by the turn-over of large bodies of the local provincial troops and naval action on the coast, met with an unexpectedly feeble resistance from the redoubtable XIXth Route Army and occupied Foochow with little or no fighting about the 16th January. Before the end of the month the rebellion had finally collapsed, the XIXth Route Army were in full retreat on all fronts, and their leaders, including Chen Ming-shu, Li Chi-shen, Chiang Kuang-nai, Tsai Ting-kai and Eugene Chen, had fled the country.
- 4. The immediate reasons for the rapid collapse of the Fukien rebellion were, no doubt, to be sought as much in the political as in the military measures taken by Chiang Kai-shek for its suppression, the former including the winning over of the provincial forces, who had no particular object in allying themselves with the XIXth Route Army and the rebel Government of Chen Ming-shu. It is probable that the newly organised air force of the National Government, whose aeroplanes made several raids into Fukien from Nanchang, also played a considerable part in destroying the *moral* of the rebel forces. In any case, whatever the true causes of the rebellion and its collapse may have been, the result was a considerable increase in the power and prestige of Chiang Kai-shek and the National Government. It was noteworthy that on this occasion public opinion throughout China and amongst the large and influential Chinese communities in Malaya and the South Seas was overwhelmingly in favour of the Nanking Government and against the rebel movement and its leaders. And it is likely that the moral support now being generally lent to the National Government by Chinese public opinion will become an increasingly important factor in the internal situation in the future.

- The final measures taken by Chiang Kai-shek for the liquidation of the Fukien rebellion included the appointment of Chen Yi, Vice-Minister of War, as chairman of the Fukien Provincial Government and that of Chiang Ting-wen, another Nanking general, who had been in charge of the punitive expedition, as Bandit Suppression Commissioner for Fukien, and also the dispersal, or amalgamation in the forces of the National Government of the XIXth Route Army. This famous force had first made a name for itself in the civil wars between the Kuomintang and the North in 1926, 1927 and 1928 and had crowned its reputation and earned the admiration of the whole country by its resistance to the Japanese at Shanghai in 1932. But at the same time, owing to its origin and political associations, it had always been a source of embarrassment to Chiang Kai-shek and the Nanking Government, who could thus congratulate themselves that these events had led, not only to the Province of Fukien passing under their direct control, but also to the elimination of this formidable and potentially dangerous force. The disappearance from the political scene of Chen Ming-shu was probably also not unwelcome to Chen Chi-tang, the rival Cantonese leader and de facto ruler of Kuangtung; for it was common knowledge that the XIXth Route Army and its leaders had a grievance against the existing Canton régime and aspired to return to their homes in Kuangtung.
- 6. As a result of the successful suppression of the Fukien rebellion, the Fourth Plenary Session of the (4th) Central Executive Committee of the Kuomintang, convened at Nanking in January, was held on due date in an atmosphere far more favourable to Nanking than seemed at one time likely to be the case. So far, however, as the results of the session were published, the only measure of importance adopted was the re-election of Lin Sen as President of the National Government for a further period of two years.
- 7. Chang Hsueh-liang, who in 1933 had been forced to resign and retire abroad following on the inglorious failure of his North-Eastern Army to defend Jehol against the Japanese invasion, returned to China early in the year and in February assumed at Hankow the post of Deputy Commander-in-chief of Bandit Suppression Forces for Honan, Hupei, and Anhui. As Chiang Kai-shek was himself concurrently Commander-in-chief of these forces (actually the principal armed forces of the National Government), the appointment was outwardly one of the first importance as deputy to the generalissimo. To what extent Chang Hsueh-liang has played an active part in his new post and the degree of military power of which he still disposes are, however, doubtful points. Possibly his real importance is no longer as great as it appears in foreign eyes. Nevertheless, in spite of the jealousy and opposition aroused by his appointment among the local military chiefs at Hankow, no overt friction has occurred; and "the Young Marshal" has continued throughout the year to play the decorative rôle of China's leading young military chief lending patriotic and enlightened support to the generalissimo. Chiang Kai-shek is, on his side, under special obligation to the Young Marshal, being bound, according to Chinese public opinion, to requite the services rendered to him by the latter at the time of Yen Hsi-shan's rebellion in North China in 1930.
- 8. Amongst the important developments during the early part of the year, though not one directly affecting the Chinese Government, was the enthronement as Emperor of Manchukuo on the 1st March of Pu Yi, the last Emperor of the Manchu dynasty of China. This event had little or no effect on the internal situation in China or on the relations between the Chinese and Japanese Governments, though the former, after having had their hands forced by manifestos of the South-West Political Council at Canton, issued a mandate denouncing Pu Yi and the other Chinese "puppets" of the new Manchukuo Empire as guilty of high treason to the State.
- 9. It was not long before Sino-Japanese relations were subjected to a further shock by the issue on the 17th April of the Japanese Foreign Office statement warning the nations of the world that China was in future to be regarded as a Japanese preserve. In this case also the reactions of the Chinese Government and Chinese press were relatively mild, the attitude generally adopted being that China, in view of her present weakness, had no alternative but to ignore these insults to her status as an independent nation and await the hour when she would

be strong enough to make suitable reply and demand the restoration of the lost North-Eastern Provinces. The Waichiaopu lost no time in issuing a counter-statement commenting on the Japanese declaration and refuting in dignified terms the Japanese claims, while the South-West Political Council at Canton also issued soon after their own declaration, couched in more violent language, denouncing the Japanese gesture as a threat to the independence of China and the peace of the Far East.

- 10. In North China two minor military revolts were successfully dealt with by the National Government early in the year. An ex-bandit general named Liu Kuei-tang, stationed in Chahar in Inner Mongolia, who had revolted in December 1933, crossed the Great Wall into the neutral zone and appeared early in January in the neighbourhood of Peking. After some desultory fighting, General Liu and his bandit troops were shepherded back to their old haunts in the mountains of Shantung, where they were finally dispersed and absorbed into the ranks of the local brigands. The other rebel in the North was General Sun Tien-ying, who, with his troops, had been ejected from Chahar after Feng Yü-hsiang's rebellion in 1933. In January General Sun's troops, who had nominally been transferred to garrison the Kokonor border, where there were neither duties for them to perform nor means for their support, came into conflict with the Kansu Moslems near Ninghsia on the Yellow River. Eventually, after inconclusive fighting had been proceeding in these remote regions for some weeks, the Central Government declared themselves against General Sun, whose forces were finally defeated and dispersed by the Government troops in the middle of March.
- 11. Apart from these minor revolts and recurrent waves of nervousness and tension caused by rumours of further armed aggression by Japan, the situation in North China remained relatively peaceful throughout the year. It will be recalled that, following the events of the early summer of 1933, General Ho Yingchin, Minister of War in the National Government, and Huang Fu, the Japanese trained politician, who had formerly occupied the post of Minister for Foreign Affairs, had been appointed to take charge of military and civil affairs in North China respectively. These appointments indicated the intention of Chiang Kaishek and the National Government to assume direct control of the situation in the North and at the same time to seek a settlement locally of outstanding questions with Japan. Amongst these local questions were the problems of the policing and administration of the neutral zone, the restoration to Chinese civil control of Kupeikou and the other passes (or rather gates) in the Great Wall, the establishment therein of customs stations, the restoration of through railway traffic between Peking and Mukden, and the resumption of postal communications between China and Manchuria.
- 12. It was known by the spring that the Japanese were pressing very hard for a settlement of these outstanding questions and threatening to take action of some kind unless more normal relations between Manchuria and North China were resumed in the near future. The Chinese Government, on the other hand, were impeded at every turn in the execution of their new policy of seeking to get on terms again with Japan by the criticisms and attacks of their internal opponents in South China. The result was a series of nervous advances under Japanese pressure, followed by the usual clamour from the South, and consequent delays, procrastinations and withdrawals on the Chinese side. In particular Huang Fu's position was one of great delicacy and difficulty and early in April he suddenly left Peking for Central China, where he remained until the autumn of the year, ostensibly on leave, but actually engaged in intermittent consultations and discussions with Chiang Kai-shek and the National Government.
- 13. In spite of Huang Fu's absence the negotiations between the Chinese and Japanese authorities in North China continued during the summer in an atmosphere of nervous secrecy on the Chinese side. These confidential discussions finally resulted at the end of June in a settlement of the question of through railway traffic by means of an agreement to run a daily through train between Peking and Mukden, an arrangement which was no doubt regarded from the Japanese point of view as only a beginning for the resumption of more normal railway communication later on. Local agreements were also arrived at for the nominal retrocession to Chinese control of the passes in the Great Wall, except

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Malanyü—though in actual fact the Japanese Kuantung army remained in full control of the line of the Wall, which, under the Tangku Agreement could not be approached by Chinese troops—and for the establishment at the gates in the Wall of sub-stations of the Chinese Maritime Customs.

- 14. Huang Fu eventually returned to Peking in September, thus disposing of many rumours that he had resigned on account of the difficulties of his position. It was assumed that he had brought with him a mandate from the Central Government for a final settlement of outstanding local questions with Japan, including the thorny problem of the restoration of postal communications between North China and Manchukuo. So far, however, no settlement of this question has been reached, although there are reasons to believe that some agreement may have been concluded for publication later. While European mails transiting Manchuria are delivered in China, the Chinese Post Office still refuses to hand mail matter over to the Manchurian authorities or to receive mails originating from Manchukuo and franked with the new Manchurian stamps bearing the effigy of the Emperor Pu Yi. In other respects, however, the atmosphere as between Chinese and Japanese in North China has been much improved, as compared with the previous year, due to the evident desire of Huang Fu and the other local Chinese authorities to conciliate the Japanese and avoid friction with the chiefs of the Kuantung army.
- 15. The relations between Nanking and Canton have continued generally unchanged throughout the year, except that, with the buffer province of Fukien passing under the control of the National Government, the armed forces of Nanking have been brought into contact with those of Canton on the northern borders of Kuangtung. It was therefore generally expected that Chiang Kaishek and the National Government would make some move towards strengthening their influence in the south. The test of the situation as between Nanking and Canton has long turned on the continued existence of the South-West Political Council, the organ through which the anti-Nanking politicians in the south, under the leadership of Hu Han-min, Tang Shao-yi, Tsou Lu, and their colleagues, advertise their opposition to Chiang Kai-shek and the National Government. The real power in the south is, however, known to reside in the hands of the military chiefs, namely, Chen Chi-tang at Canton and Li Tsung-jen and Pai Chung-hsi in Kuangsi, the first named having, it is generally believed, a secret understanding with Chiang Kai-shek. Reports of important political changes pending in the south were freely current during the first half of the year, the intention being, according to these rumours, to abolish the South-West Political Council and to establish at Canton a branch military commission, nominally under the control of Nanking, like that functioning at Peking. Whatever the true history of these intrigues and manœuvres and of the activities of various emissaries sent by Nanking to South China may have been, it seems to have been found impracticable to proceed so fast in the matter; and, down to the time of the closing of this report, there have been no developments in the situation in the south, where the politicians, while professing to recognise the National Government, continue to advertise their implacable hostility to Chiang Kai-shek.
- 16. The campaign against the Communists in Kiangsi, directed by Chiang Kai-shek himself from his headquarters at Nanchang, dragged on throughout the year, owing to the remarkable elusiveness and powers of resistance of the Red forces, and an apparent lack of enthusiasm on the part of the Government troops. In the absence of any really effective co-operation from the authorities of the adjoining provinces, the Red bands repeatedly broke out of Kiangsi in raids in different directions into adjacent areas. The Province of Fukien, though garrisoned by the forces of the Central Government, has suffered through the year from several of these raids, one of which, in the month of August, brought the Reds to the neighbourhood of Foochow and the coast. In October and November, as a result of pressure from the Government troops assisted by the economic blockade which had been put into force and the construction of new motor roads and fortified posts, the principal Red strongholds in Kiangsi, including the Chinese Soviet capital, Juikin, were one by one surrendered by the Communists, whose main force broke westwards into Southern Hunan with the apparent object of reaching Szechuan via Kueichow. One body has already passed through Hunan

and effected a junction with the notorious Red leader, Ho Lung, in the mountainous hinterland on the borders of the four provinces of Hunan, Hupei, Szechuan and Kueichow, whence they have been raiding through the last-named province and Northern Hunan. The greater part of the Reds, however, is still, at the moment of writing, engaged in heavy fighting on the Kuangtung-Hunan and Kuangsi-Hunan borders, presumably with the object of protecting their flank during their march westwards. The result of the evacuation of Kiangsi by the main body of Reds has thus been to eliminate the buffer which has existed between Nanking and Canton for several years, and which there was reason to believe neither party has been anxious to see disappear, while, on the other hand, Nanking's problems have in reality been thereby accentuated, inasmuch as the Reds have left a trail of devastated country behind them, and are now making for regions from which it will be even more difficult to dislodge them. As is usually the case, the action taken by the different provincial Governments has been to defend their own territory and shepherd the Reds on elsewhere, and no really effective effort has been made to surround them and deal with them in an effective manner.

- The rich province of Szechuan in Western China has been another area in which the Communists have shown increased activity during the year. These bands, which have infested the northern districts of Szechuan since 1933, are understood to be the remnants of the Red forces which were driven out of Hupei after the pacification of that province a year or two earlier and took refuge in the mountains of Southern Shensi and the adjoining Szechuan border. Szechuan teems with local troops, but reproduces in miniature the conditions prevailing in the various provinces of the Chinese republic in that each local general is only concerned with maintaining himself in his own area and is not prepared to endanger his own position by expending his military resources in the national interest. The result has been that, though Marshal Liu Hsiang claimed in 1933 to have driven out his principal rival Liu Wen-hui and established himself as the de facto ruler of the greater part of Szechuan, he and the generals who nominally acknowledge his authority have failed signally to deal with the repeated Communist invasions of the northern districts of the province, where the story of the year has been a dismal record of Red raids, defeats of Government troops, looted cities and fleeing missionaries. At one time in the summer the situation was so bad that great nervousness prevailed even in Chengtu and Chungking, but it is understood that conditions improved somewhat in the latter part of the year.
- 18. As regards the internal affairs of the Kuomintang and the National Government, mention was made in the last annual report of the proposal to establish during the year 1933 a National People's Assembly to advise and assist the Government during the period of "tutelage" and to convene in March 1935 a National People's Congress to discuss and adopt a permanent Constitution. These arrangements were subsequently modified by the decision to hold a National Emergency Congress in July 1933, which was in turn abandoned on account of the convening of the regular Fifth National Party Congress for the 12th November, 1933. Owing to the intrigues and opposition of the southern leaders (who believed, no doubt with reason, that all these congresses and assemblies would, if convened at Nanking, merely serve to strengthen the influence and position of Chiang Kai-shek and the National Government), it was finally decided to postpone the convening of the fifth party congress for another twelve months to the 12th November, 1934.
- 19. Public opinion in party affairs at Nanking was, during the summer, centred on the convening of this fifth national party congress in the capital on the 12th November. It will be recalled that the Constitution of the Kuomintang calls for a full congress of party delegates every two years, but that for various reasons only four such congresses have so far been held, the first at Canton at the time of the reorganisation of the Kuomintang in 1924, the second, under Communist influence, at Canton in 1926, the third under the auspices of Chiang Kai-shek at Nanking in 1929, and the fourth convened separately at Nanking and Canton in November 1931. As the date for the convening of the postponed fifth congress approached, it became evident that it was once again the subject of a violent political controversy below the surface on account of the opposition of the southern politicians to the holding of any such congress in Nanking. At first

it was announced, in August, that the question of Southern participation had been settled, that the delegates from the south-west would attend, and that the congress would certainly open on due date. Later, however, manifestos were put out by the South-West Political Council strongly criticising the proposed procedure for the congress and attacking the Government and Chiang Kai-shek on account of their internal policies and failure to resist the aggression of the Japanese. Finally, it was announced on the 25th October that the Standing Committee of the Central Executive Committee had decided to postpone the fifth national party congress, the date for the opening of which was one of the main subjects considered by the fifth plenary session of the (4th) Central Executive Committee held in Nanking in December.

- 20. During the year the Legislative Yuan has continued its labours in connexion with the drafting of the Constitution. Three drafts in all have been published, and the final, or new, draft, is being submitted for consideration to the plenary session of the Central Executive Committee referred to above. The subject has, however, excited little popular interest and as many stages have yet to be gone through before the draft Constitution comes up for ratification by the People's Congress, it is not necessary to attempt any detailed analysis at the present stage. It may, however, be mentioned that whereas under the earlier versions the position of President was to be that of a figure-head (as in France), the latest draft of the Constitution gives the head of the State much wider powers (after the American model), including the chief executive authority and the supreme command over the land, sea, and air forces. The impression is thus created that the post is being specially prepared for General Chiang Kai-shek.
- 21. The outstanding figure of General Chiang continues indeed more than ever to dominate the Government and the country, not only in military affairs, which are his proper sphere, as head of the Military Affairs Commission and Commander-in-chief of the Bandit Suppression Forces for Honan, Hupei, and Anhui, but also in all other departments of the national administration. Notable amongst the activities during the year of the generalissimo and his remarkable wife has been the launching of the New Life Movement, which aims at inculcating amongst all classes of the population the virtues of a return to the simple life and patriotism of a bygone age. Whatever the real objects of the movement may be, whether they are the reconstruction of the nation, the formulation of a new line of defence against communism, or a blind to divert public attention from the failure of the Government to resist the aggression of Japan, it has unfortunately, on occasion, led to a revival of anti-foreign feeling and interference with the sale of foreign goods—though it is but fair to add that the generalissimo himself has given no indication of countenancing these improper activities. Another movement, but one of a less reputable and open kind, believed to be sponsored by the generalissimo has been that associated with the activities of the so-called "Blue Shirts," a secret organisation understood to be modelled on Fascist lines and to be designed to serve as an instrument, and if necessary a ruthless one, for furthering the plans and ambitions of Chiang Kai-shek.
- 22. During the summer General Chiang's health was the cause of serious anxiety, and in the autumn he made a special trip by aeroplane to North China in order to undergo a thorough physical examination in the Rockefeller Foundation Hospital in Peking. The medical certificate issued stated that he was in a fairly good average state of health, but suffering from a nervous indigestion due to overwork and aggravated by bad teeth. It is noteworthy, as a sign of the times and of the increasing security of the generalissimo's position, that on this trip, though travelling unescorted and accompanied only by his wife and a small staff, he went from Nanchang via Hankow as far afield as Honan, Hopei, Suiyuan, Chahar and Shansi, and was everywhere well received and acclaimed as the leader of the State. He was accompanied as far as Honan by the "Young Marshal," Chang Hsueh-liang, with whom he paid a flying visit by aeroplane from Loyang in Honan to Shensi and Kansu.
- 23. Reviewing the general situation in China at the end of the year 1934, one can record, in spite of many set-backs and disappointments, further progress in the strengthening of the position of the National Government, whose influence, already consolidated in the Yangtse Valley, has now been extended into North and South China through the occupation by Government forces of Hopei and

Fukien. Roughly speaking the Central Government can now claim to exercise direct control through their nominees, or rather those of General Chiang, over the provinces of Kiangsu, Chekiang, Kiangsi, Fukien, Anhui, Hupei, Honan, Hopei, Shensi, Kansu, and Inner Mongolia. Of the other provinces, the de facto rulers of Shantung (Han Fu-chu) and Shansi (Yen Hsi-shan) in the north, and of Hunan (Ho Chien), Szechuan (Liu Hsiang), Yunnan (Lung Yun) and Kueichow in the south-west, profess to owe full allegiance to the National Government and refrain, as long as their personal interests are not affected, from any overt opposition to its policies. Only the southern *bloc*, comprised by Kuangtung and Kuangsi, continue openly to advertise their disapproval of Chiang Kai-shek and the present Nanking régime, though even they profess to recognise the latter as the Central Government of China. Nevertheless, the basis of the National Government remains deplorably narrow as regards its personnel, which, weakened by the withdrawal of T. V. Soong and Lo Wen-kan, tends increasingly to give the impression of serving as a mere façade for the dictatorship of General Chiang. In the meantime the generalissimo and his Government have to continue, as in 1933, to maintain their balance between the external pressure of the Japanese and the internal assaults of their domestic opponents. There seems little doubt but that they have decided on a policy of cutting China's losses in the north, seeking to get on terms again with Japan so far as may be possible without compromising the Manchurian question, and concentrating on the suppression of communism and internal reconstruction in China. This policy appears to be now in active execution, popular demonstrations of anti-Japanese feeling are being curbed and diverted into other channels such as those of the New Life Movement, and a genuine effort is being made to conciliate the Japanese. But each step forward towards an understanding with Japan is liable to be greeted by a storm of abuse from the south, where the opponents of General Chiang and the National Government, though they are themselves without any alternative policy for dealing with Japan, have reason to fear that every increase in the power of Nanking brings them a step nearer to political extinction. And it is therefore against this background of foreign aggression and internal disunion that the progress and accomplishments of the Chinese Government must be judged.

(2) Mongolia.

The past year has seen both the Japanese and the Chinese bidding for Mongol favour and the Chinese in particular seem to have become much more aware of the necessity of meeting Mongol aspirations half way. In mid-January the Central Government, after prolonged examination of Huang Shao-wu's report on his goodwill mission (see paragraphs 75 to 77 of the annual report for 1933), promulgated certain general principles for the enforcement of autonomy in Inner Mongolia. Great opposition was at once manifested to these principles by the Mongol delegates assembled in Nanking, who claimed that they were not in accordance with the agreement which had been provisionally reached during the negotiations with Huang Shao-wu in Mongolia. As a result of their representations, the Nanking Government agreed to reconsider the question of Mongol autonomy, and on the 28th February adopted certain revised principles providing for the establishment of a single Mongol Local Autonomy Political Affairs Committee, which was to be under the direct control of the Executive Yuan. It was thus designed to meet one of the main Mongol grievances, that their affairs were bandied between provincial and central Government authorities for months before any decision was reached. Another Mongol grievance was met by the before any decision was reached. Another Mongol grievance was met by the provision that the reclamation of pasturage areas for farming should be stopped; in addition, the present organisation of Leagues and Banners was to be preserved, with the altered title of League Governments and Banner Governments. On the 7th March the Nanking Government promulgated an Organic Outline laying down the Constitution of the Local Autonomy Committee which was to be set up at Pailingmiao. This Organic Outline provided that a High Directing Commissioner was to be appointed, and a provisional ordinance was issued at the same time laying down his duties, General Ho Ying-chin being chosen for the post. On the 23rd April the committee was duly inaugurated, consisting of twentyeight members, all of whom were Mongols, and Princes Yun and Te were appointed chairman and secretary-general respectively. The former is an aged cypher, who

resigned in August, Prince Kuo taking his place. Prince Te, a man of 34, has, as reported in last year's annual report, taken a very active part in the campaign for self-determination in Inner Mongolia and is recognised as leader of the movement.

- 25. In the meantime, the Japanese had not been behindhand in courting the Mongols. On the 1st March the Chief Executive of the Manchukuo was created Emperor of the Manchukuo. One of the main reasons for this change was reputed to be that it would attract the Mongol Princes through their personal allegiance to Pu Yi as the descendant of the Manchu dynasty. In addition, the new empire, at the instance of the Japanese, has continued to encourage the semi-autonomous province of Hsingan, and steps have been taken with a view to opening up rapid communication with Inner Mongolia by road and air as well as by wireless telegraphy. A bureau for the improvement of relations between friendly countries has also been set up at Dolonor and the Japanese are reported to have organised travelling medical missions to Inner Mongolia, which should appeal to the Mongols, who are as lacking in medical knowledge as in supplies. Japanese officers, moreover, are known to have paid frequent visits to the Mongol Princes, and two spent the winter of 1933 at Prince Te's palace.
- Despite these Japanese overtures it seems, however, that the leaders of Mongol autonomy are not unaware of the disadvantages of handing themselves over to the Japanese, for they realise that Japanese domination will entail more irksome regulations and stricter discipline than Chinese. They may, nevertheless, be forced to turn to the Japanese for support, if the Chinese evade their promises. There is, indeed, already evidence of this contingency occurring, for while the Nanking Government make concessions to Mongol aspirations the execution of all plans is left to the provincial authorities whose interests are strongly opposed to granting them. For instance, when members of His Majesty's Legation visited Pailingmiao in August, there were already signs that the provincial authorities had little intention of carrying out the Nanking Government's undertaking that no more pasturage should be reclaimed, the reason being that the land tax obtainable from Chinese farmers is much higher than anything that can be mulcted out of Mongol graziers. Moreover, it appears that the subsidy promised by the Central Government for the running expenses of the Local Autonomy Committee has never been paid. Excessive taxation in the reclaimed area and increasing distance from the Chinese markets at Kalgan and Kweihua are also tending to force the Mongols to search for a better market from either Russia or Japan. In October, however, General Ho Ying-chin paid a visit to Pailingmiao, and in November Chiang Kai-shek made a rapid tour of Suiyuan and Chahar Provinces, where he met Mongol representatives. It is not so far apparent whether, as a result of these meetings, the Chinese authorities will be more ready to carry out their undertakings in practice.
- 27. Little information has been available on conditions in Outer Mongolia during the course of the year, but the Chinese authorities are reported to be negotiating with the Union of Soviet Socialist Republics consul at Kalgan for the reopening of trade between Inner and Outer Mongolia. The only present contact is a so-called Sino-German trading company with offices in Kalgan, which maintains a truck service direct with Urga. They state that the communications in Outer Mongolia have been greatly improved, and that speeds of 60 miles an hour are possible on the main road to the frontier, whereas in Inner Mongolia an average of 20 miles an hour is the maximum possible. Frontier guards of Mongolians commanded by Buriats are stationed on all the roads in Outer Mongolia, and penetration by persons who are not welcome to the Soviet is practically impossible. It appears that the city of Urga itself has been greatly improved recently, and that a number of buildings in Siberian style with a cinema and a radio station have been erected.

(3) Sinkiang.

28. As a result of the civil war in Sinkiang the situation towards the end of last year was briefly as follows (see paragraph 87 of annual report for 1933). In Southern Sinkiang Chinese official authority had completely disappeared and the local Turki leaders, of whom Khoja Niaz Haji was the most influential, were generally in control of the various oases, with the exception of the New City at

Kashgar, which was still held by Ma Chan-tsang and the Tungans. In Northern Sinkiang Liu Wen-lung and General Sheng Shih-tsai at Urumchi, and General Chang Pei-yuan in Ili, maintained some sort of nominally Chinese administration, but were carrying on intermittent hostilities with the Tungan leader, Ma Chungying, who controlled the Turfan and Hami regions. Late in December, however, General Ma Chung-ying was reported to have been badly defeated by General Sheng Shih-tsai's troops near Urumchi and to have been compelled to hand over Turfan and to withdraw along the road towards Southern Sinkiang. During the course of these hostilities, General Chang Pei-yuan refused to support General Sheng Shih-tsai, but he is reported to have been assassinated by his own followers during a mutiny early in January and his troops subsequently to have surrendered to the Provincial Government. These events left General Sheng Shih-tsai the effective ruler of Northern Sinkiang, in which position he has remained up to the time of writing. The only change that has occurred is that Liu Wen-lung has resigned, apparently disgruntled, and his place as provincial chairman has been taken by Li Jung, a member of the Sinkiang Provincial Government Council.

- 29. To turn to Southern Sinkiang. In October and November 1933 the Turki leaders attempted to organise an "Independent Islamic Republic of Eastern Turkestan," under the leadership of Khoja Niaz Haji. Although this Government carried on nominally until early in February 1934, it was never much more than a paper organisation. It was, moreover, divided into two camps. There were, on the one hand, those, such as Khoja Niaz himself, who favoured close relations with Russia (chiefly as a means of obtaining arms) as well as relations with Nanking. On the other hand, the extreme Islam party favoured complete independence from Russia as well as from Nanking. The arrival of Ma Chung-ying's Tungan troops from Northern Sinkiang after their defeat at the hands of Sheng Shih-tsai rather than internal dissension was, however, the cause of the downfall of the republic and with it of Turki dominance in Southern Sinkiang. Late in December 1933 Aksu fell to Ma Chung-ying's Tungan advance guard, and early in February 1934 these troops combined with the Tungan forces in Kashgar New City, captured Kashgar Old City, and drove the Turki forces towards Yarkand and Khotan. During this fighting His Majesty's consulategeneral was fired on by the Tungans, there being several British casualties, including the wife of His Majesty's consul-general. Full apologies were received from the Tungan commander as well as from Ma Shao-wu, the former Taoyin of Kashgar, who had, in 1933, retired with the Tungans into Kashgar New City. At the same time, a strong protest was made to the Chinese authorities in Nanking, who expressed their sincere regret. Including this incident, His Majesty's consulgeneral reported that known losses to British subjects in lives and property during the disorders in 1933 to 1934 amounted to fourteen killed, two missing, four wounded, and goods valued at 267,055 rupees. This is, however, admittedly not a complete or a final list. Ma Chung-ying, at this juncture, gave out that his policy was adherence to Nanking and opposition to the Union of Soviet Socialist Republics, whose servant, he said, Sheng Shih-tsai had become.
- 30. The Tungan control of Southern Sinkiang was, however, scarcely longer lived or more effective than the republic whose place it took, for Sheng Shih-tsai's troops gradually followed up their victories in Northern Sinkiang by defeating Ma Chung-ying's troops at Karashar early in the year, again near Aksu in April, and in the beginning of July, Maralbashi, some 150 miles from Kashgar, was occupied. At this point General Ma Chung-ying fled and is reported, despite his previous anti-Soviet declarations, to have crossed the border into the Union of Soviet Socialist Republics. On the 20th July Sheng Shih-tsai's troops arrived in Kashgar and Ma Shao-wu was officially reinstated as Taoyin. Later, on the 7th August, General Liu Pin arrived from Urumchi by air, having been appointed the Provincial Government's chief representative in South Sinkiang for both civil and military affairs.
- 31. The Tungans had, meanwhile, withdrawn to Khotan and in September sent delegates to Kashgar to discuss the possibility of a peaceful settlement. It seems, however, that no satisfactory settlement could be reached. Nevertheless since the evacuation of the Tungans from Kashgar, no major hostilities have, so far as is known, occurred; but intermittent cases of freebooting and brigandage in the course of which Ma Shao-wu himself has been severely wounded, together

with the unsettled state of the local administration at Kashgar and the anxiety of local merchants that the Sovietisation of trade is imminent, have combined to make the existing peace precarious.

When His Majesty's Minister was in Nanking in October, the Minister for Foreign Affairs volunteered the statement that the civil war in Sinkiang was at an end and that the Central Government were in close touch with the provincial authorities. He added that the Central Government wished to see the province developed economically with foreign co-operation, but that the provincial authorities had been instructed that they were not to enter into any negotiations with foreign Powers without the authority of the Central Government. He made it clear that the Soviet Government in Moscow as well as the Soviet Ambassador in China had been informed accordingly. This statement seems to have been made largely for reasons of face for the Central Government realising their inability, for the present at any rate, to guide the course of affairs in Sinkiang have, in fact, accepted what has occurred with as much grace and outward claim to authority as possible. Nevertheless so far as relations between the Union of Soviet Socialist Republics and Sinkiang are concerned, the fact is that in recent years Sinkiang has almost become economically, if not politically, a Soviet dependency and that Sheng Shih-tsai owes his successes mainly to the Soviet arms and aeroplanes that he has acquired. As things are, there is, therefore, no great prospect of the Chinese Government regaining effective control in Sinkiang and the dangers arising out of Soviet domination of this province are likely to be a matter of concern to His Majesty's Government in the United Kingdom.

(4) Tibet.

33. On the 17th December, 1933, the Dalai Lama died. In view of the special position which the late Dalai Lama had made for himself, having been the effective and independent ruler of the country since 1912, this event was of cardinal importance in recent Tibetan history. The main characteristics of the late Dalai Lama's rule had been internally his own personal dominance of secular as well as religious affairs, and in foreign policy the close relations which he had cultivated with His Majesty's Government in the United Kingdom involving severance with China. It is too early as yet to forecast what change, if any, will result from his death, but the record of events in 1934 shows that all those who have suffered as a result of the late Dalai Lama's policy are making determined efforts to restore their fortunes.

34. In internal affairs the Government of the country has been carried on by the Regent who was appointed in January, the Lönchen or Prime Minister, and Kashag or Cabinet Council. The main feature of the internal situation in the first half of the year seems to have been a struggle for power between the Government on the one hand and the National Assembly on the other. The Assembly has often, in the past, held a preponderating influence over State affairs and is usually under the domination of the three great monasteries: Ganchen, Sera, and Drepong. The late Dalai Lama, however, had in recent years tended to act without summoning the Assembly and had, moreover, steadily restrained the leading clerics from interfering in secular affairs. The Assembly's bid to regain influence came to a head on the 10th May when a number of specific demands were put forward including one for consultation on all administrative questions, whether internal or external. The Government, however, arrested the leader of this agitation, confiscated his property, and ten days later put his eyes out. This drastic action, combined with other arrests, seems to have curbed the Assembly for the time being.

35. In the field of foreign affairs the Chinese Government at once realised that the death of the Dalai Lama presented them with the opportunity for a settlement with Tibet, for which they have been waiting since the breakdown of the Simla Conference in 1913. Accordingly, by a Chinese Government mandate issued on the 12th January, General Huang Mu-sung, Vice-Chief of the General Staff and special Pacification Commissioner for Sinkiang in 1933 (see annual report for 1933, paragraph 85), was appointed head of a mission to Tibet, as special representative to offer condolences on the death of the Dalai Lama. At the same time the Vice-Minister for Foreign Affairs informed His Majesty's

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Legation confidentially that the mission would take the opportunity of discussing outstanding questions. No date, however, was set for the time of the departure of the mission. The Chinese Government no doubt wished first of all to ascertain the Tibetan Government's reaction, since no official Chinese representatives had been in Lhasa since the expulsion of the Chinese in 1912. In the event the Tibetan Government agreed to receive the mission, and when early in March His Majesty's Minister told General Huang in Nanking of our readiness to give facilities for travel via India, the general, in thanking His Majesty's Minister, intimated that his mission would consist of an advance party which would travel via India to make the necessary preparations, and that he himself would travel overland. The advance party of seven members, including attendants, actually sailed from Hong Kong on the 21st March and reached Lhasa in May. Some idea of the effort which the Chinese Government are making to ensure the success of the mission may be gained from the fact that the advance party took with them over 100 boxes of presents, and on arrival in Lhasa presented 50,000 dollars for expenses on the Dalai Lama's tomb and similar amounts to the three great monasteries of Sera, Drepong, and Ganden. General Huang and his party of thirty-seven set out early in April and arrived in Lhasa on the 28th August. From reports received to date it appears that on arrival General Huang Mu-sung proceeded to pay official calls on Tibetan officials and make lavish donations to the powerful monasteries; but so far it is not known to His Majesty's Legation what subjects he discussed in Lhasa or what the outcome of his negotiations with the Tibetan Government has been. The Chinese mission has, however, already obtained facilities for return to China via India, and General Huang Mu-sung left Lhasa at the end of November.

- In addition the Tashi (Panchen) Lama, who has been an exile from Tibet since 1924, has, since the death of the Dalai Lama, been active in arranging for his return to Tibet. In order no doubt to secure the goodwill of His Majesty's Government in the United Kingdom he has been careful throughout this year to keep in close touch with His Majesty's Legation. In January His Serenity passed through Peking on his way to Nanking from Inner Mongolia to discuss projects for his return to Tibet with the Chinese Government, and at this time his representatives in Peking intimated that His Serenity might be able to leave for Tibet in about two months' time. The latter was accordingly informed that, if the Tashi Lama wished to travel via India, all facilities would be granted. In March His Majesty's Minister was told by His Serenity in Nanking, however, that the date for his return to Tibet had not been settled, but that the two representatives, the Anchin Hutuktu and Wang Lo-chieh, whom he had sent to Lhasa last year to discuss matters were on their way back to report to him. It subsequently appeared that their negotiations in Lhasa had not been entirely satisfactory; but when in July His Serenity again passed through Peking on his way to Inner Mongolia, he informed His Majesty's Legation that the Anchin Hutuktu and Wang Lo-chieh were shortly going back to Lhasa to continue discussions and that as they intended to travel via India he would be grateful for any facilities that could be granted to them. His Majesty's Legation were duly approached for facilities for these two representatives as well as a suite of thirty followers, together with 400 pieces of baggage which were said to contain articles for the use of the Panchen Lama. It would appear, therefore, that His Serenity has some concrete hope of returning to Tibet in the near future and it is, in fact, reported that there is a general desire among all classes in Tibet that he should do so.
- 37. On the Sino-Tibetan marches the Yangtze River (Chinsha) appears to have remained the *de facto* boundary. The only actual hostilities that have taken place occurred in March over the question of the Ta Chin Monastery in Kanze; but they did not last long, and after two months a truce agreement was signed on the 17th May. This agreement seems to have patched up matters on the border, temporarily at least, since General Huang and the Chinese mission were able to pass safely through Kanze and Chamdo on their way to Lhasa.
- 38. Sir Charles Bell made an unofficial journey to Tibet during the latter half of this year. It is understood, however, that he did not visit Lhasa itself, since the Tibetan Government felt that in view of the presence of the Chinese mission it would be undesirable for him to do so.

39. Early in the year His Majesty the King approved the elevation of the status of the British Minister Resident in Nepal to that of an Envoy Extraordinary and Minister Plenipotentiary, and the reception of a Nepalese Envoy Extraordinary and Minister Plenipotentiary in London. This did not have any apparent reaction in China, unless it was instrumental in rousing the Chinese Government to send the consul-general at Calcutta in June on a special mission to Katmandu. Similar Chinese missions had, however, visited Katmandu in 1930, the first official intercourse since the establishment of the republic, and in 1932.

(5) Communism.

- 40. During the first part of the year the Communist situation in China remained much the same as in 1933; the same areas were under Communist control, and the neighbouring country was still liable to sporadic incursions. The area under the main Red forces in the Kiangsi–Fukien district was, however, gradually being reduced in extent by Chiang Kai-shek's army, and his policy of attrition compelled the Communists during the summer to resort to an extensive raid towards Foochow. This raid was beaten off and in the last months of the year the continued pressure of Government forces resulted in further advances, and the capture was reported of areas which had been in Communist hands since 1930. Further details of the anti-Communist campaign are given in the section under Military Operations, from which it will be seen that there are grounds for guarded optimism.
- 41. As regards the spread of Soviet doctrine in China, there have during the past year been no signs to give the Communist International grounds for hoping for a wide acceptance by the Chinese of communism in the Russian sense. In Shanghai a series of successful raids have been carried out during the year by the police of the International Settlement, French Concession and Chinese city on known Communist addresses, of which at least one was of considerable importance. As a result the organisation of the Chinese Communist party in Shanghai has been seriously weakened. Much of the information leading to these raids has been procured by special Nanking Government agents, and there is no doubt but that the Communist problem is being taken seriously by the Chinese authorities. The Blue-shirt Organisation, which is reported to be under the direct control of General Chiang Kai-shek, has also been active in anti-Red work. In this connexion it is interesting to note that in September the National Government decorated several of the International Settlement police force for their efforts against communism in Shanghai. The efforts of those organisations functioning in China, which depend for their direction and funds on the Communist International, have been equally non-productive during the past year, although they continue to receive large subsidies from abroad. In North China particularly, their work is becoming more difficult and dangerous as Japanese influence in the area increases.

(6) Military Operations,

42. The main military operations in 1934 have been those conducted with varying success against Communists and bandits. Chiang Kai-shek's anti-Communist campaign in Kiangsi had very little chance of success as long as he was not in full control of the three forces operating against the Red concentration from the north, east and south. The Cantonese in the south were inclined to maintain a passive resistance provided communism did not spread into their territory, and the XIXth Route Army in Fukien joined the independence movement in that province. The provincial troops, mostly reformed brigands, threw their lot in with Tsai Ting-kai's regulars, and Chiang was obliged to suspend operations in Kiangsi to put down the rebellion. He rapidly concentrated about 100,000 troops on the Chekiang border and invaded Fukien with about 55,000. The forward concentration of the invading force was at Pucheng, where it advanced to join the 56th Division, which had remained loyal and held Kienning for the Central Government. The garrison of Yenping, 30 miles to the south-south-east, consisted of local levies with no love for the XIXth Route Army, who promptly surrendered on the approach of the National forces. The invading force then turned aside to deal with the 7th Fukien Division, which put up some slight show of resistance and afterwards descended the Min River to Foochow.

During the advance there were some slight skirmishes with units of the 60th and 78th Divisions. Tsai Ting-kai, seeing the odds against him, withdrew to the south, and the independence movement ignominiously collapsed.

- The XIXth Route Army was purged of its senior officers and shipped off to Northern Honan for reorganisation. Chen Yi, Vice-Minister of War and a stout adherent of Chiang Kai-shek, was installed as Chairman of Fukien, and the generalissimo could at last count on two of the attacking forces out of three to carry out his orders against the Red areas in South Kiangsi. The line of advance against Juichin, the Communist capital, is via Tingchow from the east and through Shihcheng from the north. The Government forces are, however, moving very slowly and are consolidating their gains by improving communications and putting captured villages in a state of defence. The rest of the Province of Fukien has, however, never properly been cleared up, and the northern districts have harboured large numbers of disaffected troops who were only too ready to join the Communists in their raids in search of salt and munitions. In August the pressure from the north and south-east obliged the Reds to make a diversion, and a column from the Shaowu area reached Yuki only 70 miles from Foochow. Simultaneously some of the old provincial troops who had never been rounded up in the Funing area again took up arms and began to move towards Santuao. Foochow itself was threatened, and the Central Government was forced to recall the old XIXth (now VIIth) Route Army from Honan to stabilise the situation.
- 44. Progress has undoubtedly been made in the vicinity of the Communist centre at Juichin. The main danger, however, appears to be that the action of the Nanking forces may dislodge rather than suppress the Communists. The Chinese are always averse to any drastic action. A division which revolts is still kept on the roster in the hopes that some day it may return to its allegiance, and it is customary to leave a way of escape for any adversary. Provincial authorities are far too parochial, and rarely bestir themselves to suppress an enemy if they can sub-let the responsibility to a neighbour. They content themselves with shepherding subversive elements through their territory, leaving them free to select a new base of operations in the next province. At the end of September Hsiao Ko, with the bulk of the Communists in South-West Kiangsi, broke away westwards and crossed Hunan into Kweichow, with the intention of joining up with Ho Lung in South-Western Hupeh and eventually with the Reds in Szechuan.
- 45. The Communist situation in that province is sufficiently serious without the influx of fresh blood from the outside. At the beginning of the year an organised drive with six Route Armies was undertaken to drive them back on the Shensi border and if possible to surround them. The direction of operations was entrusted to Liu Hsiang, but in spite of newspaper reports of successive victories very little was achieved. Petty jealousies among the various commanders rendered co-operation impossible, and finally the VIth Army deserted to the enemy. The Reds have now extended the area under their control to the Kialing River, and Chengtu itself is threatened.
- 46. Since the Jehol campaign, North China has been extremely free from military operations. The bulk of the Young Marshal's troops were drafted down to Hankow to rejoin him on his appointment as Vice-Commander of Bandit Suppression, and the only disturbance of the peace in Hopei was created by the passage of Liu Kwei-tang and about 800 of his ex-brigands. This band of ruffians changed sides several times during the Jehol campaign and its aftermath, and, as the cold weather approached, decided to leave the highlands of Chahar for a more congenial climate. They passed from north to south of Hopei through 60,000 troops, looting as they went, completely unmolested by the garrisons. Entering Honan they struck westwards for Shensi, then doubled back on their tracks parallel to the Lung-Hai Railway as far as Northern Kiangsu. It then appeared likely that they would make for their old haunts in the mountains of Shantung, but they were headed off by the energetic Governor Han Fu-chu. A large number of troops and provincial levies were mobilised against them and in five weeks the band was broken up.

47. A minor campaign also took place on the upper reaches of the Yellow River. Sun Tien-ying, who had been swept into Chahar by the Japanese advance, attempted to force his passage to Ching Hai, where the Nanking Government had offered him a post to get rid of him. He was, however, opposed by the Chairmen of Ching Hai and Kansu, as well as the Governor of Ninghsia. As he declined to listen to the orders of the Central Government to withdraw, he was declared a rebel, and the Governors of Suiyuan and Shansi were ordered to round him up. Very little fighting took place in this suppression campaign, and it is probable that Sun received some pecuniary inducement to retire. His troops were disposed of by disbandment or incorporation with those of the National Army.

(7) Shuntien Piracy.

- 48. On the 17th June Messrs: Butterfield and Swire's steamship Shuntien, while on her regular run between Tientsin and Shanghai, was seized at 10·30 p.m., six and a half hours after sailing from Tangku, by a band of thirty to forty pirates, who were on board as passengers. The pirates immediately gained control of the ship, and the only shooting occurred when the officer of the watch on the bridge was wounded while resisting capture. The pirates directed the ship's course towards the mouth of the Yellow River, where she was stranded on the afternoon of the 18th June. In the meantime, the passengers in the ship had been relieved of their valuables, and the pirates took as hostages five British captives, three of whom, Lieutenant J. D. Luce, R.N., Lieutenant P. L. Field, R.N., Mr. G. D. Nicholl, were passengers, and two, Messrs. G. L. Brand and H. McD. Watson, were ship's officers, as well as about twenty-one Chinese, and one Japanese subject.
- 49. Shortly after the departure of the pirates the steamship Shuntien got under way for Chefoo, and immediately communicated by wireless with the Commander-in-chief at Weihaiwei, stating what had happened. Destroyers and an aircraft carrier were without delay despatched to the scene. At the same time strong representations were made to the Chinese Government in Nanking as well as to the provincial authorities of Hopei and Shantung, whilst representatives from His Majesty's Legation proceeded to Tsinan on the 19th June to press the Governor of Shantung to take immediate steps to secure the safe release of the British captives. On the morning of the 20th June aeroplanes from the aircraft carrier, who were searching the locality, were fired on by the pirate junks and retaliated. The pirates then despatched the Japanese captive in a sampan for Tientsin, and one British captive with a Chinese in another boat with instructions to make their way to Tsinan in order to negotiate for the release of the remaining captives. The former arrived in Tientsin on the 23rd June; the latter were almost immediately picked up by British aeroplanes. In the afternoon of the same day messages were dropped to the pirates demanding the return of the remaining British captives, failing which they were warned that their junks would be bombed. This message was effective, and the remaining British prisoners were released. Thereupon the British naval forces were withdrawn. It was not until more than a month later that the majority of the Chinese prisoners were reported to have been set free, and so far none of the looted property has been recovered.

II.—FOREIGN RELATIONS.

(A) British Empire.

(1) United Kingdom.

· 50. On the 26th February the Hon. Sir Alexander Cadogan arrived in Shanghai to take up his appointment as His Majesty's Minister in China, and on the 6th March presented his credentials in Nanking to President Lin Sen, Chairman of the National Government. The leading members of the Chinese Government, in conversation with His Majesty's Minister, all emphasised the friendly relations which now exist between the Chinese Government and His Majesty's Government and their desire to see that they should be maintained. In fact, during the course of the year and up to the time of writing, relations

have remained undisturbed. On the 15th January Wing-Commander R. P. Willock, R.A.F., arrived to take up his appointment as air attaché to His Majesty's Legation, with headquarters in Shanghai. In May Mr. E. M. B. Ingram, C.M.G., O.B.E., left China on completion of his period of service as counsellor to His Majesty's Legation, and on the 1st July Mr. R. G. Howe arrived in Shanghai as his successor. In August Mr. L. B. G. S. Beale, C.B.E., His Majesty's commercial counsellor, left China on home leave, Mr. A. H. George assuming his duties as acting commercial counsellor.

- 51. Authority was sought and received from the Foreign Office to make the necessary alterations to the sub-Legation buildings in Nanking, to enable members of His Majesty's Minister's staff to use them for longer visits than have in the past been customary. Arrangements have also been made for His Majesty's consul-general's house to be taken over as the official residence of His Majesty's Minister when at Nanking and of his representative in his absence.
- 52. On the 1st January a note was received from the Waichiaopu drawing attention to the fact that the third decennial period of the Sino-British Commercial Treaty of 1902 ended on the 25th July, 1933, and stating that since this treaty, like the Treaty of Tientsin of 1858 (see annual report for 1931, paragraph 142), had become out of date, they desired to conclude new, equal and reciprocal treaties to take their place. After instructions had been obtained from the Foreign Office, the Chinese Government were informed in a note of the 19th May that, in accordance with their declared policy, His Majesty's Government in the United Kingdom would give most sympathetic consideration to any specific and concrete suggestions that the Chinese Government might care to The Waichiaopu replied by a note of the 24th May that the two particular matters which they considered needed revision were the provisions dealing with extra-territoriality and with existing rights of coastal and inland A formal acknowledgment only was returned to the Chinese Government in June stating that the Chinese note had been referred to His Majesty's Government for consideration. Up to the time of writing the Chinese Government have not pressed this matter further, and since it appears doubtful whether they have any real desire to enter into serious negotiations at the present time, no further communication has been addressed to them by His Majesty's Legation. In the event, however, of their returning to the charge, it was decided that, while intimating our willingness to explore further the possibility of negotiating a new commercial treaty, we should give the Chinese Government clearly to understand that the negotiations on the subject of extra-territoriality were carried by His Majesty's Government in 1931 to the furthest possible point, beyond which it was not possible to proceed until the Chinese Government had made similar progress in their discussions with the other Governments concerned, and were in a position to implement throughout China any treaty which might be reached; and that, the position still remaining unchanged, the question of extra-territoriality could not be raised in any way under cover of negotiations for a new commercial treaty.
- 53. Several matters affecting His Majesty's armed forces in China have arisen this year. The General Officer Commanding raised the question of transferring the brigadier either from Shanghai or from Tientsin to his staff in Hong Kong. No decision has, however, been reached on this question up to the time of writing. During the course of the summer, when British troops were in Shanhaikuan, the local Japanese authorities informed them that they could no longer use the ground on the Manchurian side of the Great Wall for training purposes without first obtaining permission of the Manchukuo officials. It was considered by the Foreign Office that it would involve a loss of prestige to try to reach any compromise with the Japanese on this subject, since His Majesty's Government did not admit that the Japanese military had any right to impose restrictions of any kind upon the movement of British forces in North China. It was, therefore, decided voluntarily to abandon for the time being all training on the Manchurian side of the Great Wall. A verbal communication was accordingly made to the Japanese Legation in Peking, as well as to the Japanese Minister for Foreign Affairs in Tokyo, that this decision had been taken in order to avoid all risks of disturbing friendly relations between the British and Japanese military authorities in North China.

- 54. In April a letter was received from the Waichiaopu laying down the procedure whereby the import of all supplies, other than munitions of war, for foreign naval and military forces stationed in North China was to be restricted and controlled. The general consensus of opinion among the Powers affected was that to agree to any such restrictions imposed by the Chinese Government would render the existence of any foreign forces in China impossible. In reply to a request for instructions, the Foreign Office ruled that, while general international law and practice could not be held strictly to entitle members of His Majesty's armed forces stationed in China to claim duty-free treatment for articles imported for their personal use, the best should be done for their general convenience. Acting in accordance with the discretion thus given, and after consultation with the United States Legation, the Waichiaopu were informed, in a memorandum of the 1st November, that it had been found impracticable to accept the new proposed regulations, that British authorities had always taken, and would continue to take, proper precautions to ensure against any misuse of supplies imported for His Majesty's forces, but that, if there were concrete grounds for believing that abuses had arisen, they would be prepared strictly to investigate such complaints, with a view to taking appropriate measures. The Waichiaopu replied that the proposed regulations did not conflict with Sino-foreign treaties, that they were not in any way impracticable, and that, as the date for their enforcement, namely, the 1st January, 1935, was imminent, they trusted that His Majesty's Legation would reconsider their attitude. The question of what answer is to be made to the Waichiaopu and whether any compromise proposals should be put forward is under consideration at the time of writing.
- 55. Various points concerning the 1929 contract for British naval assistance to China have arisen this year. In May Admiral Chen requested the appointment of a successor to Captain H. T. Baillie-Grohman, who had left China in April 1933 on the completion of his term as head of the British naval mission to China, provided for in the 1929 contract. Arrangements were accordingly made for the appointment of Captain J. A. V. Morse, D.S.O., R.N., who is due to arrive at Shanghai on the 31st December. The Admiralty reconsidered their decision, made last year, not to accept any further Chinese officers for training with the British navy, and an agreement was reached providing facilities for the training of an additional number of Chinese officers on amended lines. Five Chinese officers accordingly sailed for England during the course of the summer. In addition, arrangements were made, at the request of the Chinese Government, for the renewal for one year from the 16th November of Commander R. N. Stopford's appointment as liaison officer with the Chinese officers being trained in England. On information being received that the Chinese Government had given a contract to the Japanese for the construction of a cruiser, enquiries were made of Admiral Chen, since the Chinese Government had expressed their intention in the 1929 contract of purchasing vessels and naval material in Great Britain. Admiral Chen explained that the arrangements made with the Japanese were only for the completion of a cruiser laid down by them three years ago, before Sino-Japanese hostilities had necessitated the suspension of all work. He added that, while he would be only too willing to place orders in Great Britain, the naval budget had been cut to the bone, and that any question of purchases would have to be ruled out for as far ahead as he could see.
- 56. In March the Vice-Minister for Foreign Affairs approached His Majesty's Minister verbally about the Chinese Government regulations for the importation of arms into China and, in referring to the provisions requiring the issue of a permit by the Central Government and its endorsement by the Chinese representative from the country of export, stated that cases of unauthorised importations by provincial authorities, especially by Kwangtung, had occurred. He admitted that there was no specific complaint against His Majesty's Government, but wished to enlist our co-operation. It was pointed out that British authorities everywhere co-operated strictly in the application of the Chinese regulations, and it subsequently appeared, after enquiries had been made by His Majesty's Legation, that we were, in fact, the only large arms-exporting country to do so. In April a note was received by the foreign Legations, including His Majesty's Legation, from the Waichiaopu in the sense of the Vice-Minister for Foreign Affairs' verbal representations, and the Chinese Minister

in London also addressed a note to the Foreign Office. These various communications were received just at a time when His Majesty's Government were considering warning the Chinese Government that, unless they made their regulations effective against all countries, we might have to reconsider our attitude. Since, however, it was learned in reply to enquiries made that the countries chiefly concerned with the import of arms into China had expressed their intention to adhere strictly to the Chinese regulations, it was decided that any reconsideration of our attitude that might be necessary should be postponed until it appeared whether the present move by the Chinese Government represented a sincere attempt to apply their regulations effectively.

- 57. In April the Chinese Government announced their decision to make a final payment to the British Eastern Extension Cable Company and the Danish Great Northern Cable Company in respect of the North China Cable Loan Agreement of 1904, and at the same time informed the cable companies of their intention of immediately taking over the Shanghai, Chefoo and Taku cables. The companies complained that sufficient notice had not been given to make the necessary arrangements to transfer the cables, but agreed that the action decided upon by the Chinese Government was strictly in accordance with the terms of the 1904 Loan Agreement. The companies, therefore, after first trying to enlist the good offices of His Majesty's and the Danish Legations, finally decided to hand over the cables without demur.
- 58. In June the Chinese Government placed a postal ban on a British monthly magazine entitled *Oriental Affairs*, published in Shanghai and edited by Mr. H. G. W. Woodhead, C.B.E. On enquiry by His Majesty's Legation, it was subsequently explained by the Waichiaopu that the reasons for the ban were that the tone of the articles had been consistently hostile and injurious to the Chinese Government, and that the magazine had been carrying on subtle propaganda on behalf of Manchukuo. The Chinese officials at the same time made it clear that they did not want to make this question a cause celèbre between the Chinese Government and His Majesty's Government, and explained that they were prepared to lift the ban as soon as the editor offered amends. Mr. Woodhead, however, refused to publish anything by way of apology, but in the September issue of his magazine finally made a statement that his articles had only been intended as fair and frank comment. The Chinese Government intimated that this statement would not be sufficient, as no expression of regret had been made. However, although the ban has not yet been withdrawn in theory, it appears that in practice Mr. Woodhead is not experiencing much difficulty in passing *Oriental Affairs* through the posts. Interference by the Chinese with the compilation of his *China Year Book* has also raised an additional issue.
- 59. On instructions from the Foreign Office, a request was made to the Chinese Government regarding the question of the status of persons born of Chinese parents in British territory for further assurances in respect of the issue of denationalisation certificates, as well as for specific rulings on a number of points relative to the Chinese Nationality Law. The reply from the Waichiaopu was not wholly satisfactory, and instructions have been requested from the Foreign Office whether any further action is required vis-à-vis the Chinese Government and whether we can now proceed to define our attitude towards this question more precisely, for the information and guidance of His Majesty's consular officers in China.
- 60. After several years of continued pressure on the leaseholders concerned by His Majesty's consulate-general at Hankow, the position was reached on the 1st June that all holders of British Crown leases in the former British concession areas at Hankow and Kiukiang had exchanged these leases for Chinese deeds of perpetual lease. It was accordingly possible on the 27th October to effect an exchange of notes cancelling the head agreements of March 1861 and August 1898 under which the Chinese Government had leased the above-mentioned areas to His Majesty's Government.
- 61. His Majesty's consul-general at Hankow has also this year initiated negotiations for the regularisation of the affairs of the Kuling Estate. This land was originally leased to a British subject, Mr. E. S. Little, in 1895 and an

extension was acquired in 1905. During the past two decades the estate has been administered by a foreign body called "The Kuling Estate Council," who have granted sub-leases for a number of lots. A draft agreement has now been put forward by His Majesty's consul-general at Hankow to the provincial authorities of Kiangsi for their approval, which will enable lot-holders to obtain Chinese deeds of perpetual lease in place of these sub-leases and will create an administration, on the lines of that established in the ex-British concession at Hankow, under a Chinese director, assisted by a Sino-foreign advisory committee.

- 62. On the 1st October five members of the China Inland Mission were captured in Kueichow Province, three of whom, Mr. and Mrs. Hayman and Miss Emblem, were British subjects, the remaining two, Mr. and Mrs. Bosshardt being Swiss citizens. Mrs. Hayman and Mrs. Bosshardt were released at once and Miss Emblem was also set free before the middle of October. In response to our representations the Chinese authorities have undertaken to do all that is possible to effect the release of Mr. Hayman with Mr. Bosshardt, who, however, still remain in the hands of the Communists. Apart from this incident and the Shuntien piracy, no other case has occurred up to the time of writing of British subjects being kidnapped in China during 1934.
- 63. Relations with the South-Western political leaders have remained normal during the course of the year, and although a number of important trade questions have been discussed, such as the business tax and the kerosene oil regulations dealt with in the commercial section of this report, they have not led to any serious repercussions. In May the Canton Provincial Government requested a loan of a torpedo gunner's mate for instruction duties in connexion with the torpedo equipment of coastal motor boats, and with their concurrence the approval of the Central Government was sought. The Nanking Government, however, refused to sanction this proposal, which consequently fell through. Moreover, tentative approaches were made by representatives of the Kwangsi leaders for financial assistance to help in the industrial development of the province, but the proposals put forward were of a very general kind and have not yet led to agreement on any concrete projects.
- 64. Negotiations regarding the case of the Anglo-Chinese College at Swatow have continued throughout the year, but up to the time of writing no settlement has been reached. The position now is that the Canton provincial authorities have made an offer to pay 25,000 dollars as compensation for expropriation, and efforts are still being made to persuade them to increase this offer.

(2) Canada.

- 65. On the 8th July the Canadian Government Trade Commissioner for North China, Mr. Paul Sykes, left Tientsin for Canada, and Mr. A. K. Doull took charge of his office.
- 66. Canadian trade relations with China have been adversely affected by the increase on the 16th December, 1933, by the Chinese Government of their tariff rates on wheat, which forms the major item of Canadian exports to China. The Canadian Government Trade Commissioner at Shanghai informed His Majesty's commercial counsellor that, while this action by the Chinese Government would be a great blow to trade between the two countries, there were no grounds on which to base a protest so long as the same increased rates were applied to all countries.
- 67. Colonel Cosgrave, Canadian Trade Commissioner at Shanghai, left China on the 18th November to act in a similar capacity in Australia.

(3) Commonwealth of Australia.

- 68. Australian interests were, like Canadian, affected by the increase on the 16th December, 1933, of tariff rates on wheat, which forms the major item of exports to China from the Commonwealth.
- 69. On the 25th April the Right Hon. J. G. Latham, P.C., C.M.G., K.C., M.P., Deputy Prime Minister and Minister for External Affairs, arrived in China at the head of an Australian Far Eastern Mission to neighbouring

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countries in the Pacific, the object of which was primarily goodwill and not trade. After spending a few days in Shanghai, the mission visited Nanking as the official guests of the Chinese Government, and during the course of the meetings and entertainments arranged Mr. Latham took full opportunity of successfully carrying out his mission. From Nanking the mission came to Peking for a short stay before returning to Shanghai to catch their ship to Japan on the 7th May. As a result of his investigations, Mr. Latham stated that he was contemplating recommending the appointment of two Commonwealth Government Trade Commissioners, one at Hong Kong and the other at Shanghai. On the way back to Australia from Japan the mission took the opportunity of their ship's stay in Hong Kong to visit Canton, where His Majesty's consul-general arranged for them to meet the chief Southern leaders.

(4) Union of South Africa.

70. Mr. A. T. Brennan was appointed Trade Commissioner for the Union of South Africa in the East, with headquarters at Batavia. His duties are to include a thorough investigation of the Union's trade possibilities with China, and the Chinese Government have at the instance of His Majesty's Legation undertaken to afford facilities and assistance as occasion arises.

(5) Burma.

- 71. The question of the Burma-Yunnan frontier, which had lain dormant since 1929 (see paragraphs 242–243, annual report, 1929), was brought to the fore again this year by the despatch in January of an expedition from Burma to the Wa States adjoining the southern undemarcated frontier, to examine the possibilities of developing mines. Express instructions had been given to the civil officer in charge of the expedition not to cross the westernmost frontier claimed by the Chinese Government, the so-called Liu Chen line, without prior reference to His Majesty's Government in the United Kingdom; but despite assurances given to the Chinese authorities Yunnan provincial troops were moved towards the area, and early in March a protest against the expedition was made by the Central Government, who maintained that it had entered Chinese territory. His Majesty's Minister, on proceeding to Nanking shortly after his arrival in China, accordingly took the opportunity of reassuring the Chinese Government that, while His Majesty's Government in no way recognised the Liu Chen line, the expedition had not, in fact, crossed it. His Majesty's Minister further agreed to refer to His Majesty's Government a tentative suggestion by the Chinese Government that a fresh attempt should be made to settle the frontier in this area.
- 72. While this suggestion was under consideration, reports from the expedition indicated that Chinese troops and officials had crossed the line regarded by His Majesty's Government as the frontier, namely, the line demarcated by Sir George Scott in 1900, and a strong protest was therefore made to the Chinese authorities in April. By this time, however, the geological experts attached to the expedition had collected sufficient evidence to satisfy themselves that there were no commercially workable mines in this area and they accordingly withdrew. Nevertheless, it was clear that the expedition, once having penetrated into this previously unadministered area, could not, for political reasons, retire and that the area would therefore have to be brought under some form of permanent control.
- 73. At this juncture it seemed not impossible that a serious situation might arise; for, despite the protest made in April, bodies of armed Chinese continued to operate in the area between the Scott and Liu Chen lines, and a number of engagements had to be fought against them by the expedition on the British side of the Liu Chen line. In addition, both the Central Government and the Yunnan provincial authorities intimated their intention of sending missions to investigate in the disputed area. In mid-June, therefore, a further strong protest was made to the Minister for Foreign Affairs in Nanking, who was urged to issue immediate orders for the withdrawal of all bodies of troops that had crossed the Scott line, and to hold up the despatch of any mission to the disputed area pending negotiations for the settlement of the frontier. At the same time he was told that His Majesty's Government were fully prepared to agree with the Chinese Government's suggestion for an agreed delimitation of the boundary, and proposed to

that end that as a first step the principles which should underlie delimitation should be discussed at a preliminary conference in Nanking. In reply, the Minister for Foreign Affairs undertook verbally to look into the question of troops in the disputed area, and to consider carefully the proposed scheme for a settlement of the boundary question. Meanwhile, he stated that he was in general agreement with the method proposed, and intimated that, if negotiations went forward, instructions might be sent to the Chinese Investigation Mission not to proceed into the disputed area. At the end of the month a note was received generally confirming the Minister for Foreign Affairs' verbal statements, and accordingly a further memorandum was communicated to the Waichiaopu in July stating that His Majesty's Government were ready to take urgent steps to appoint representatives for a conference in Nanking. At the same time the attention of the Chinese Government was once again drawn to the fact that raids by armed Chinese to the west of the Liu Chen line were still occurring despite the Minister for Foreign Affairs' undertaking. It appears, however, that the Chinese raiders were, for the most part, brigands and disbanded soldiers over whom the Chinese authorities can have little control, and although the expedition has from time to time had to fight minor engagements against them, no serious hostilities have so far resulted.

- 74. After careful consideration it seemed to His Majesty's Legation that the best hope of reaching an agreement at the proposed conference at Nanking would be to get the Chinese to admit that the basis of the settlement should be the relevant paragraphs of article 3 of the Anglo-Chinese Agreement of 1897, and to agree to demarcate on the ground the line resulting from the main geographical indications such as the fixed points and watershed there mentioned. Majesty's Minister accordingly suggested that before a conference was finally arranged, His Majesty's Legation should first approach the Waichiaopu informally and find out whether there was any chance of the Chinese Government accepting a settlement on this basis. This suggestion was approved by His Majesty's Government, and Sir Eric Teichman proceeded to Nanking early in August to discuss matters informally with the Vice-Minister for Foreign Affairs. The latter at once informed Sir Eric Teichman that as negotiations for a settlement of the boundary question had been opened, the Chinese Government Investigation Mission, which had reached Yunnan, would not enter the disputed area. From the discussions which ensued it appeared that while a settlement on the basis proposed by His Majesty's Legation might not in a general way be unacceptable, the Chinese Government held that there were certain inaccuracies in the text of the 1897 agreement, which made it impossible to use it as a strict basis for demarcation. In short, the geographical indications could not, in the Chinese Government's opinion, be reconciled with the geographical names given in the agreement, and while we might wish to have the boundary demarcated exclusively in accordance with the former, the latter favoured the Chinese. explanation of this stand by the Chinese Government was that one of the main causes of the failure of the Sino-British Frontier Commission to demarcate this section of the boundary in 1899 and 1900 arose over the situation of a range referred to in the English version of the treaty as the Kongmingshan, the Chinese Government claiming that there was no such range where the treaty states it to be, but that there was a Kungmingshan much further to the west, along which the boundary should run.
- 75. It was, however, felt that enough progress had been made in the discussions to make it unnecessary to hold a preliminary conference in Nanking. Accordingly, on the 25th October, His Majesty's Minister presented a memorandum to the Minister for Foreign Affairs informing him that His Majesty's Government were prepared to revert to the Chinese proposal for a joint boundary commission, and suggested that it should be set up at once under a neutral chairman selected by the President of the Council of the League of Nations. It was proposed that the first term of reference of the commission should be to fix on the map the line resulting from the geographical indications given in article 3 of the 1897 agreement. The line so fixed should form the basis for subsequent negotiation of any adjustments of the kind contemplated in article 6 of the agreement, so as to avoid the intersection of tribal territories or villages. If it were found necessary a conference could be convened for these subsequent negotiations, and, in order to facilitate their task, the second term of reference of

the commission should, it was proposed, be to report, in the light of their local examination of the ground, on any cases in which questions appeared to them to arise of modification on the basis of mutual concession. The Chinese Government replied in a memorandum of the 3rd November agreeing generally to the proposed procedure, but suggesting that the chairman's duties should be simply to advise the joint commissioners and not to arbitrate on any points of difference that might arise between them. As regards the terms of reference, the Chinese Government, as was to be expected, proposed that the joint commission should be instructed to demarcate the line in accordance with geographical names as well as geographical indications, and, moreover, should be authorised to recommend to their Governments a line embodying such adjustments as they thought fit, rather than that they should keep quite separate their duties in respect of demarcation and of recommending adjustments.

- After the Chinese memorandum had been duly considered by His Majesty's Government, His Majesty's Legation replied by a memorandum dated the 4th December stating that as regards the chairman's duties His Majesty's Government considered it essential that he should exercise all the functions usual in such cases, including that of a casting vote, and that they were unable to accept the Chinese suggestion that he should be confined to giving advice and assistance. As regards the terms of reference of the proposed commission, His Majesty's Government agreed with the Chinese Government's suggestion that the first term of reference should be to demarcate the line prescribed by the 1897 convention, giving relative weight to the geographical names as well as to the geographical indications there mentioned. On the other hand, since the primary duty of the commission should be to interpret the agreement, His Majesty's Government considered that the commission's duties in respect of demarcation and of recommending adjustments should be kept entirely separate. Any modifications of the general treaty line which the commission might, in accordance with the second term of reference, suggest should, therefore, in His Majesty's Government's view, be negotiated subsequently, if necessary at a conference.
- 77. The Chinese Government replied on the 15th December that they were prepared to accept the views of His Majesty's Government with regard to the duties of the neutral chairman. The Chinese Government also expressed general agreement with the other suggestion put forward by His Majesty's Government, except that as regards the first term of reference they expressed the opinion that in performing the task of treaty interpretation the commission should attach equal importance, instead of giving their relative weight, to all the geographical names and indications referred to in the relevant articles of the 1897 convention. The views of the Chinese Government are under consideration by His Majesty's Government, but in view of the conciliatory nature of the Chinese reply there is reason to hope that an agreement will shortly be reached with regard to the terms of reference of the commission.

(6) Straits Settlements and Federated Malay States.

- 78. The Chinese Government having appointed as a consul élève at Kuala Lumpur the son of a Chinese who had been banished from Malaya in 1932 on account of his Kuomintang activities, the Governor officially informed the Chinese consul-general at Singapore on the 31st January that this consul élève was persona non grata. After some discussion a compromise was reached, whereby the Governor, for his part, agreed to cancel his official communication of the 31st January to the Chinese consul-general, while the Chinese Government undertook to withdraw the consul élève, who accordingly left on transfer to Johannesberg as vice-consul at the end of May.
- 79. The Chinese Minister for Industries arrived in Singapore on the 1st May during the course of his tour to the South Seas, leaving for the Netherlands East Indies on the 11th May. He stated that the object of his tour was to study the condition of overseas Chinese and to encourage them to buy Chinese goods.
- 80. On the 12th February legislation was enacted to facilitate the entry of certain classes of Chinese labour into Malaya by authorising the Colonial Secretary to issue permits for immigrant ships from China to bring to Malaya

additional labour outside the present quota. It was feared that this permit system might give rise to difficulties since it threatened to interfere with the profits of the immigrant brokers in China, who might avenge themselves by provoking an anti-British agitation by representing that the scheme involved indentured labour. No actual trouble is so far reported to have occurred, however, at Swatow and Amoy from which places most of the immigrant labourers are recruited.

(7) Hong Kong.

- 81. In April the Minister for Industries visited Hong Kong on his tour of the South Seas and held conferences with Hu Han-min and other political personages as well as with local Chinese merchants, who, it is reported, represented that Hong Kong products should be given tariff preferences on entrance into China. It is understood that replies to these representations were non-committal.
- 82. The decision was reached that the scheme for the construction of a public park in Kowloon City and the evacuation of Chinese residents (see annual report for 1933, paragraph 143) should go forward and an offer was communicated to the latter to provide them with new sites and houses in return for their present property. All the Chinese, except one recalcitrant, eventually accepted this offer; but, nevertheless, the Chinese Minister for Foreign Affairs, in June, telegraphed to His Majesty's Minister urging that the scheme should be abandoned on the grounds that it was contrary to treaty stipulation and was causing alarm to the Chinese residents. In reply, a memorandum was communicated to the Minister for Foreign Affairs expressing the view that there was no question of a breach of treaty and that the Chinese Government must have been misinformed about the attitude of the Chinese residents.
- 83. A conference for the revision of the Canton-Kowloon Railway Agreement was held in Hong Kong in July, further details of which are given in the section of this report dealing with Railways.
- 84. In November a conference was held in Hong Kong attended by the Secretaries for Chinese Affairs of the Governments of Hong Kong and of the Straits Settlements as well as by the Chinese counsellor to His Majesty's Legation and His Majesty's consul-general at Canton.

(B) Other Countries.

(1) Japan.

- 85. This year, for the first year since 1930, the Japanese have not resorted to direct military action to gain any objective in China. Nevertheless, they have succeeded by other means in making some progress towards their various immediate aims, such as the establishment of working arrangements between Manchukuo and China and the improvement of their trade relations with this country.
- 86. In the first two or three months of the year, however, the Japanese apparently refrained from pressing the Chinese very hard for any immediate satisfaction of their demands. In fact, in January the Japanese Legation told His Majesty's Chargé d'Affaires that, in their opinion, it was hopeless to do so for the moment. In any event, the enthronement on the 1st March of Pu Yi as Emperor of Manchukuo, together with the fact that the Japanese garrisons at Tientsin and Peking selected this particular moment to carry out large-scale manœuvres, might have made it difficult for the Chinese Government, in the face of Chinese public opinion, to come to any overt agreement with the Japanese at this time. By the spring, however, there were signs that the Japanese were losing patience, and early in April they must have begun to exert considerable pressure, for it was then that General Huang Fu, who had negotiated the Tangku Armistice Agreement in May 1933, left Peking to confer with the Central Government.
- 87. Moreover, on the 18th April, shortly after his departure from Peking, a member of the Press Bureau of the Japanese Ministry for Foreign Affairs made an informal verbal statement to the Japanese press announcing that Japan would oppose any attempt on the part of China to avail herself of assistance from any other country to resist Japan. For example, it was explained, Japan saw

objection to joint operations by foreign countries in the name of technical and financial assistance and to China being supplied with military aeroplanes or being lent military instructors and advisers. From this and other evidence, it seems that the statement was issued largely to anticipate the publication of Dr. Rajchman's report to the League of Nations, and was also aimed against M. Monnet's plans for the foundation of the China Development Finance Corporation as well as against the part played by the United States of America and Italy in civil and military aviation in China. Whatever its immediate causes, the statement could only be taken primarily as a warning to China, and, secondarily, to the League of Nations and to interested Powers, that Japan regarded China as her preserve and insisted on being consulted about any action foreign countries might contemplate in China. This statement was calmly received by the Chinese Government, whose reply was couched in the most moderate terms. Its effect outside China, however, seems to have been far beyond Japanese expectations, and in reply to representations made by His Majesty's Ambassador in Tokyo, as well as by his United States colleague, assurances were given that the Japanese did not intend to violate any of their treaty engagements. explanatory statement was handed by the Gaimusho to the press on similar lines. The sting in the original declaration, namely, that Japan claimed to be the sole arbitrator of what action by foreign Powers in China was or was not legitimate, was, however, neither withdrawn in the discussions with His Majesty's Ambassador nor in the press statement. Shortly after the issue of this Japanese declaration of policy, Wang Ching-wei sent a message to His Majesty's Minister that he would much appreciate his presence in Nanking at an early date. During the discussions with His Majesty's Minister in Nanking early in May, the Minister for Foreign Affairs pointed out the difficulty with which the Chinese Government were faced in that the opening of any negotiations with the Japanese on any basis might well be interpreted as de facto recognition of Manchukuo.

- 88. On the 8th June an incident occurred which looked as if it might lead to a serious crisis, for on that day the Japanese vice-consul at Nanking, Mr. Kuramoto, disappeared in mysterious circumstances. It was suspected that he might have been kidnapped. However, five days later, when the danger of some direct action by the Japanese seemed imminent, Mr. Kuramoto was discovered wandering in a dazed condition on the Purple Mountain near Nanking. The Japanese consul-general at Nanking told His Majesty's Minister's representative in the capital that Mr. Kuramoto had been found to be suffering from brain trouble; that he had been sent to Japan, and that the Japanese Government regarded the incident as closed.
- 89. From now onwards the Chinese Government began gradually and without any publicity to find means of meeting the Japanese demands. On the 1st July an agreement was reached for the resumption of through railway traffic between Manchukuo and China. It was emphasised that this agreement did not imply recognition of Manchukuo and, in order to give point to this, a special organisation called the Eastern Tourist Bureau was created at Shanhaikuan, as the result of an arrangement between the China Travel Service and the Japanese Tourist Bureau, to operate the through service. Early in July also the Chinese tariff was revised in such a way as to give advantage to various items in which the Japanese were especially interested. In August, moreover, an official notification was published by the Tientsin customs authorities announcing the opening of customs stations on the passes in the Great Wall between China and Manchukuo. In the following month General Huang Fu returned to Peking after an absence of five months. Since then it is known that active negotiations have been in progress regarding the question of the restoration of through postal traffic with Manchukuo. Other questions concerning North China, in particular those connected with the demilitarised zone provided for in the Tangku Armistice Agreement, have similarly been the subject of discussion.
- 90. To sum up: While the Japanese have grounds for moderate satisfaction at the record of their diplomatic achievements in China in 1934, the Chinese Government may at least look back on this year with some feeling of relief. They were faced with the difficult problem of going slow enough to avoid offending their own public opinion and fast enough to stave off any further direct Japanese action. For the first time since the 1931 crisis they achieved a certain measure

of success in handling this delicate situation, in spite of continuous opposition and criticism on the part of the south-west provinces.

(2) Russia.

- 91. Both the Minister for Foreign Affairs in March and Chiang Kai-shek in May, in the course of conversation with His Majesty's Minister, discussed the possibility of China being forced by Japanese pressure to ally herself with the Union of Soviet Socialist Republics. They both seemed, however, to be fully aware of the dangers and disadvantages to China of such an alliance and did not appear to consider that this question was one for immediate decision.
- 92. The counsellor of the Soviet Embassy told His Majesty's Minister in November that no progress at all had been made this year with the proposal for a Sino-Soviet Pact of Non-Aggression, and he seemed to think that the subject was dead.
- 93. He said that Sino-Soviet trade had improved slightly this year: Russia had imported a little more tea from China, and the Russian trade in salted fish, which had been hit by the anti-Japanese boycott, since it was assumed in China that all salted fish was of Japanese origin, had now slightly recovered.
- 94. The question of Sino-Soviet relations is also referred to in the sections on communism and Sinkiang.

(3) United States of America.

- 95. The United States Legation continued in 1934 to act in close co-operation with His Majesty's Legation in all matters affecting the interests of the two countries.
- 96. In reply to the Chinese Government's request of December 1933 for a revision of the Sino-United States Commercial Treaty of 1903, the United States Legation, on instructions from the State Department, addressed a note to the Waichiaopu on the 13th January expressing their willingness to open negotiations and enquiring what specific questions the Chinese Government had in mind. The Waichiaopu answered in a note of the 18th January in similar terms to a note later addressed to His Majesty's Legation, regarding the Sino-British Commercial Treaty, that extra-territoriality and inland and coastal navigation were the matters to which they attached the greatest importance. The United States Minister on the 10th April returned a formal acknowledgment to this communication, pending reference to the State Department, and in conversation with His Majesty's Minister in June expressed the view that the Chinese Government had been chiefly anxious to place on record their desire for treaty revision, and that at the present time they did not necessarily desire to enter into active negotiations. In fact, up to the time of writing, the Chinese Government have not pressed the matter further, and the United States Legation have, therefore, sent no further communication on the subject to the Waichiaopu. If the Chinese Government, however, bring forward this matter once more, the United States Legation have received instructions from the State Department to take a similar line to that proposed by His Majesty's Legation.
- 97. Questions connected with the United States Cotton-Wheat Loan of 1933 are dealt with in the Finance section of this report.
- 98. In May a United States missionary, Howard A. Smith, was captured by Communists at Pengshui on the Szechuan border. In July he succeeded in escaping entirely through his own initiative.
- 99. In May the United States embarked on a silver buying policy which had immediate repercussions on the currency situation in this country (see section on Finance). The Chinese Government made urgent representations to the United States Government; but it appears that, while expressing their willingness to keep in mind the considerations put forward by the Chinese Government in

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carrying out their silver policy, the United States Government made it clear that they were unable to depart from it.

- 100. The United States Minister informed His Majesty's Minister confidentially in July that the Chinese Government had refused to agree to the establishment of a Sino-United States Claims Commission on the grounds that, if such a commission were constituted for dealing with United States claims, similar commissions would have to be set up to deal with the claims of other nationals. The Chinese Government had, however, said that they were prepared to do what might be possible in regard to United States claims, and in reply to their request for particulars the United States Legation had sent in a list of some 650 claims totalling 16 million to 17 million dollars.
- 101. Early in October the United States Minister left China on home leave, and Mr. Clarence E. Gauss, counsellor of the United States Legation, assumed charge of the Legation.

(4) France.

- 102. The French Minister, M. Wilden, who had left China on home leave at the end of 1933, returned in November. In his absence, M. Hoppenot, the counsellor of the French Legation, acted as Chargé d'Affaires.
- 103. During the course of the year negotiations continued on the outstanding points concerning the Sino-French Indo-China Treaty which was signed in 1930, but which has not so far been ratified. The main obstacle to ratification by the French Government still is that the latter consider that the terms of the treaty itself do not give them an equal return for the advantages which the Chinese would thereunder acquire in Indo-China. They have accordingly been pressing the Chinese to embody in the annexes to the treaty, which deal with commercial matters, some compensating economic concessions for Indo-Chinese products on entry into China, such as, for example, for coal from Tonkin and rice from Southern Indo-China. The French Legation state, however, that so far little, if any, progress has been made towards obtaining the desired economic concessions.

(5) Germany.

- 104. So far as is known, no major matter has been under negotiation between China and Germany in 1934, the German Legation being chiefly occupied with questions connected with the engagement of German advisers and current commercial matters.
- 105. In April General von Seeckt returned to China at Chiang Kai-shek's invitation, and is understood to have acted as a special adviser on military matters. On his arrival, General Wetzel, who has been in charge of the German military mission since 1930, returned to Germany and General Falkenhausen is now in charge of the mission. No doubt largely as a result of the existence of the mission, German firms continue to sell large quantities of arms to the Chinese Government.

(6) Italy.

- 106. Italian activities have again been chiefly centred on the development of aviation and the sale of Italian machines and material in China.
- 107. In September an agreement was announced between the Italian and Chinese Governments for the raising of the Legations in both countries to the status of Embassies. His Majesty's Government in the United Kingdom at once pointed out to the Italian Government that this action was in direct contradiction to a specific assurance given in May 1933 to the effect that they would not take this step before first consulting His Majesty's Government. It appeared, however, that this assurance had been a verbal statement made by the head of a Department in the Italian Ministry for Foreign Affairs not directly responsible for Chinese affairs. It was therefore decided that no useful purpose would be served by continuing our representations. As a result, however, of enquiries from the French, United States and Japanese Governments, it was found that

they all agreed with His Majesty's Government that the time was not opportune to follow the Italian lead. The French and United States Governments, moreover, undertook not to take this step without first consulting with His Majesty's Government, while the Japanese Government promised to give due warning before doing so. It is announced that Signor Lojacono, the first Italian Ambassador to China, will arrive in this country at the beginning of the year.

(7) Netherlands.

108. In February the Netherlands Minister went home on leave, returning to China in May.

109. The Netherlands Legation have, as in 1933, been largely concerned in following the affairs of the Chefoo Harbour Improvement Commission on account of the interest which the Netherlands Harbour Works Company has in the proposed schemes for the improvement of the harbour.

(8) Belgium.

110. On the 25th August a special mission of His Majesty King Leopold III arrived in China to announce to the President of the Chinese Republic the new King's accession to the throne. The leader of the mission, Baron Emmanuel Janssen, and the Belgian Minister to China were awarded the Grand Cordon of the Order of the Brilliant Jade, and General Chiang Kai-shek and Mr. Wang Ching-wei received the Grand Cordon of the Order of Leopold.

(9) Turkey.

111. A Treaty of Friendship with China was signed at Angora on the 4th April providing for the reciprocal reception of diplomatic representatives and the subsequent conclusion of a convention to regulate consular and commercial relations. Ratifications were exchanged at Geneva on the 17th August and, under article 4, the treaty came into force on the fifteenth day thereafter. On the 11th November the treaty was registered with the League of Nations, and, by a mandate of the 16th November, General Ho Yüch-tsu was appointed Chinese Minister to Turkey. Under an arrangement with the Turkish Government, the appointment of a Turkish Minister to China will, it is understood from the Waichiaopu, await the prior arrival of the Chinese Minister in Turkey.

(10) Persia.

112. The Persian Government having decided to open a consulate in Shanghai, Mirza Hussein Khan Key-Ustuwan arrived in May to take up his post as Persian consul. He is believed to be the first Persian official to be appointed to China since the downfall of the Sassanid dynasty in the 7th century.

(11) Greece.

113. The Government of Greece appointed an honorary consul-general in Tientsin in December 1933, and during the summer an honorary vice-consul in Shanghai. These are the first consular representatives to be appointed by Greece in accordance with article 2 of the Sino-Greek treaty of 1929, which provided for mutual appointments of consuls in both countries.

(12) Treaties.

(a) Treaties with Secondary Powers.

114. In April a report once again appeared in the press that the Chinese Government were planning to negotiate an economic treaty with Siam, but in reply to enquiries of the Waichiaopu, it was ascertained that this report was misleading, since the Siamese Government had no intention of negotiating with China until Siam had concluded treaties with the Great Powers.

115. Treaties, &c., negotiated and entering into force in 1934.

(b) Tabular Statement.

With—	Place and Date of Signature.	Subject	Place and Date of Exchange or Deposit of Ratifications.	Date of Entry into Force.	Remarks.
Turkey	Angora, April 4, 1934	Treaty of Friendship	Geneva, Aug. 17, 1934	On the 15th day after ratification,	Registered with League of Nations on November 11,
United King-dom	Exchange of notes, Nan- king,October 27, 1934	Ex-British Concession areas at Hankow and Kiukiang	Lautérolte Lautérolte Lautera	i.e., Sept. 1, 1934 Oct. 27 , 1934	1934.

(13) League of Nations.

116. In January Dr. Rajchman, the chief technical delegate appointed by the League of Nations in July 1933 as liaison agent between the National Economic Council of China and the competent organs of the League of Nations, sent to Geneva an interim telegraphic report on his activities. Subsequently, in April, he returned to Geneva to present a full report on his mission in China from the date of his appointment until the 1st April. The report was divided into eleven chapters, discussing in detail the history of the National Economic Council, agriculture, cotton, silk, water conservancy, roads, health, education, and methods proposed for technical collaboration through the League. Under each of these heads, activities, progress and projects for future development were reviewed. In addition, mention was made of the work of the League advisers appointed since 1931 to help in these various fields. The report was well received in China, but in view of the feeling of distrust which Dr. Rajchman personally had aroused, particularly in Japan, it was decided that he should not return to China as liaison agent. M. Haas, who previously acted as secretary to the Lytton Commission, has been appointed in his place.

When, in August, the Union of Soviet Socialist Republics intimated their readiness to accept membership of the League of Nations at the September session of the Assembly, on condition that they received an invitation and were assured of a permanent seat on the Council, the French Government proposed preliminary action by themselves, the Italian Government and His Majesty's Government in the United Kingdom, in approaching the remaining members of the Council, of whom China was one. The Chinese Government were accordingly sounded, and, in reply to enquiries, the Vice-Minister for Foreign Affairs stated that, as regards the question of admission of the Union of Soviet Socialist Republics to membership of the League of Nations, the Chinese Government were in complete agreement. As regards the election of the Union of Soviet Socialist Republics to a permanent seat on the Council, the Vice-Minister for Foreign Affairs said that the view of the Chinese Government was that, if Russia were considered to be entitled, by reason of her size and power, to a permanent seat on the Council, China claimed a permanent seat on similar grounds. The Chinese Government would not, however, press the question of a permanent seat at the present time; but, he added, her temporary seat lapsed this year, and the Chinese Government were very anxious to be re-elected for a further period and would be extremely disappointed if they failed to obtain this objective.

118. In the event, however, China was not re-elected to a semi-permanent seat at the September session, Turkey taking her place. This caused keen disappointment, which was expressed not only in the vernacular press, but also by an official spokesman of the Waichiaopu. The general effect of the spokesman's comment was that the League had now become a purely European organisation, and that it was incumbent on the League, if it were to preserve its healthy state, to fulfil China's hope of re-election at the earliest possible date. These views were echoed in the press, with the rider that, since China was

entitled, by reason of her size and population, to a permanent seat, she should now direct her efforts to obtaining one rather than re-election to a temporary seat. When His Majesty's Minister visited Nanking in October, the Minister for Foreign Affairs, on two occasions, raised this question and requested that His Majesty's Government should be informed of the importance attached to it by the Chinese Government. He added that he had been in communication with the Acting President of the Council and that the Chinese Government hoped that there might be a possibility of an extra semi-permanent seat being created, with the understanding that China should be elected to it.

(14) International Settlement at Shanghai.

(a) Sino-Japanese Armistice Agreement.

119. The Japanese continued to keep a close watch on the movement of Chinese troops through the Shanghai demilitarised area and to insist that advance notice should be given in each case. In March, moreover, they forced the Chinese to undertake in writing to comply with their requirements in respect of prior notice as well as of the stationing within the demilitarised area of Chinese gendarmes for the protection of the Shanghai–Nanking Railway. The documents were subsequently communicated to the neutral members of the joint commission for their confidential information.

(b) Extra-Settlement Roads.

- 120. The prospect of reaching a solution of the extra-Settlement roads problem in the near future did not look bright at the beginning of the year. The main obstacle to progress, namely, the Japanese insistence on their claim to a special position in the proposed police force and the Chinese refusal to recognise any such claim, still remained and it seemed that the Chinese had no particular wish to see it surmounted. Negotiations, however, were continued between the Shanghai Municipal Council and the Japanese consul-general, as well as between the Council and the Chinese municipal authorities, and by May the foreign interests achieved a measure of agreement on the police question and a redraft of the proposed agreement was accordingly drawn up in consultation with the Japanese consul-general. This enabled the council to resume negotiations with the Chinese municipal authorities, and on the 25th May the redraft was handed to the Secretary-General of the City Government, who expressed verbally his personal view that there was nothing objectionable in it.
- 121. In the meantime, however, a further difficulty arose over the important question of the area to which the agreement was to be applied. Negotiations on this issue are still actively in progress, but so far no final agreement has been reached.

(c) Chinese Courts in the International Settlement.

- 122. While complaints of delays in the conclusion of cases and in obtaining execution of judgments still continue, it appears that the situation has to some extent been remedied by the Supplementary Regulations and Points of Procedure, issued in the summer of 1933 by the Minister of Justice. In reply to enquiries made in June, the Vice-Minister of Justice intimated that the revision of the Code of Civil Procedure had been completed and submitted to the Legislative Yuan for approval and promulgation. The revision had been undertaken on general grounds, particularly with a view to eliminating frivolous appeals and expediting the execution of judgments. It appeared, however, that the Legislative Yuan had themselves initiated a revision of the Criminal Code and that they wished to hold up approval of the revised Code of Civil Procedure until work on the Criminal Code was completed. For this reason, presumably, the revised Civil Code has not up to the present been promulgated.
- 123. Two notes were received from the Waichiaopu in August protesting against the refusal of the Shanghai Municipal Council to allow the service of summonses issued by the Special District Court in respect of the prosecution by individuals of members of the municipal police force for acts done in their official capacity. In a note of the 1st November, His Majesty's Minister replied enclosing a copy of a letter from the municipal council to the Special District Court setting out their views in full. These views, with which His Majesty's Minister stated

he was in general agreement, were that the council had no desire to shield any member of the police force who might be guilty of improper conduct, but that members of the police force were under the land regulations immune from personal action in respect of acts done in the execution of their duty and that the council's refusal to allow the service of summonses for prosecutions arising out of such acts did not constitute a breach of the court agreement.

124. Similar notes from the Waichiaopu have been received by the other signatories of the Court Agreement, namely, the French, United States, Norwegian, Netherlands and Brazilian representatives, who all returned replies on the same lines as His Majesty's Minister's note of the 1st November. It appears, however, that considerations of "face" are involved in this controversy owing to the connexion with the conclusion of the agreement of the Vice-Minister for Foreign Affairs, Mr. Hsü Mo. It may consequently not be easy to arrive at a solution.

(d) Factory Legislation.

125. The Chinese delegate to the International Labour Conference at Geneva called at the Foreign Office in July with a view to enlisting the support of His Majesty's Government in the United Kingdom in overcoming the deadlock in the negotiations between the Chinese authorities and the Shanghai Municipal Council regarding factory inspection. It was explained that while His Majesty's Government might be ready to use their influence with the council if suitable occasion arose, the latter was not a British body and that the question seemed eminently one for local discussion between the foreign and Chinese Administrations. No substantial progress in these discussions has, however, been made up to the time of writing.

(e) Telephones.

126. The controversy which arose last year between the Shanghai Municipal Council and the Chinese Telegraph Administration concerning underground cables has remained in abeyance, pending some solution of the extra-Settlement roads question.

127. In January the Ministry of Communications tentatively tried to enlist the help of His Majesty's Legation in the negotiations between the Chinese Telegraph Administration and the Shanghai Telephone Company for the replacement of their present temporary arrangements in respect of the telephone service in the outside roads by some permanent agreement. It appears, however, that while the Shanghai Telephone Company are prepared to consider any reasonable proposals, the Chinese Telegraph Administration have never put forward any concrete proposals. It was, accordingly, decided to let the matter rest until the Chinese authorities again approached His Majesty's Legation, and it seems that a final solution will scarcely be practicable until some agreement regarding the extra-Settlement roads has been reached between the council and the Chinese authorities.

(f) Pilotage.

128. The question of the possible modification of the Pilotage Regulations of 1868, which affects not only Shanghai but other ports in China, has formed the subject of negotiations between the Chinese Government and the interested powers during the course of this year and is dealt with in the section on shipping.

III.—RAILWAYS.

129. The situation with regard to Chinese railways, more particularly as regards defaults in the service of British loans, shows little improvement. With the exception of the Shanghai–Hangchow–Ningpo Railway and the Shanghai–Nanking Railway loans, no geniune attempt has been made either to meet current charges or to pay off arrears, and total indebtedness remains much what it was last year. In the following paragraphs a general survey of the position of various railways is given:—

- 130. In accordance with the arrangement made between the British and Chinese Corporation and the Ministry of Railways in 1933, the service of the Shanghai–Hangchow–Ningpo Railway Loan has been met in part from 40 per cent. of the withdrawals from the balance-in-hand of the Peking–Mukden Railway. The other 60 per cent. continues to be retained by the Ministry and no payments have been made in respect of the Fengching Loan, which is also secured on the surplus earnings of the Peking–Mukden line. On the 6th October a loan agreement entitled the Chinese Government 5 per cent. Shanghai–Hangchow–Ningpo Railway Completion Loan of the 23rd Year was initialled by the Ministry of Railways on the one part and by the British and Chinese Corporation and the China Development Finance Corporation on the other for 16 million dollars. The loan will not only be devoted to the completion of the line but also to paying-off the Shanghai–Hangchow–Ningpo Railway Loan of 1908.
- 131. Payments of interest on the Shanghai–Nanking Railway Loan are now being regularly made, but, up to the present, five annual instalments of principal and three half-yearly payments of interest, to a total of approximately £800,000, are in default, and the position is far from satisfactory. As on the other Chinese railways, reckless capital expenditure, extravagance of management, and overstaffing, have reduced the finances of the line to a deplorable condition.
- 132. On the 15th September a new working agreement was signed to regulate the relations of the British and Chinese sections of the Canton–Kowloon Railway, one of the main provisions of which was that an increased percentage of earnings should in the future be paid to the Chinese section. Thereupon the Ministry of Railways issued an order that the revenue derived from this increased percentage should be devoted to the service of the 1907 loan, but even now there is little prospect of these services being promptly met. Arrears of principal and interest still amount to approximately £1,300,000.
- 133. Accumulated arrears of principal and interest on the British portions of the two Tientsin–Pukow Railway Loans now amount to over £2,335,000, and payments into the Special Deposit Account opened in 1932 are many months in arrear, though the earnings of the line are larger than ever before and are steadily increasing.
- 134. Though the competent departments of the Chinese Government now definitely acknowledge the obligation under article 9 of the Tientsin–Pukow as well as the Hukuang Loans to substitute from customs revenues an equivalent for the *li-kin* which has been abolished, they continue to state that the customs revenues are inadequate to meet the charges made on them. With regard to the Tientsin–Pukow and other similar railway loans, we have now protested specifically against payments made from customs revenues in priority to these railways, since *li-kin* was abolished in 1931, from the increase of customs revenue which accrued by the raising of the tariff in February 1929, and have enumerated all loans in respect of which payments have been made during the year ended the 30th June last.
- 135. In the case of the Hukuang Railways Loan, defaults on which amount to nearly £2,800,000, we have, owing to the American attitude (see paragraph 210 of annual report for 1933), been unable specifically to claim this priority of charge, and we have jointly with the French and American Legations merely called upon the Chinese Government in general terms to implement their obligations under articles 8 and 9 of the agreement and make available the customs revenues obligated for the service of this loan.
- 136. No payments have been made in respect of the Pukow–Sinyang Railway and the Nanking–Hunan Railway advances. With regard to the latter, we have pressed for repayment of the original advances, and of the arrears of interest thereon, on the grounds that the Chinese Government, by handing over the properties of the old Anhui Provincial Railway, and by contracting with others for the construction of the line from Nanchang to Pinghsiang, have unilaterally abrogated the terms of the 1914 agreement with the British and Chinese Corporation and are therefore bound under article 21 of the agreement to make repayment of these advances.

- 137. Payments under the agreement made in 1933 for the settlement of the claims of British creditors of the Tientsin–Pukow Railway, for materials supplied (see paragraph 218 of annual report for 1933), are now being regularly made and arrears are being steadily paid off. Tentative unofficial negotiations for a similar settlement of British claims for materials supplied to the Peking–Hankow Railway have been entered into, but are not progressing satisfactorily. The settlement on reasonable terms of these and other British materials debts has, however, been prejudiced by the extraordinarily easy terms accepted by some American and Japanese claimants in respect of similar debts. There appears to be no doubt that early this year American creditors of the Peking–Suiyuan, Peking–Hankow, and Lunghai Railways accepted settlements on the basis that all interest be cancelled, the original principal doubled, and payment effected in 700 to 800 instalments by means of post-dated cheques covering a period of sixty to seventy years; clauses being inserted to the effect that the instalments payable monthly should be increased if the affairs of the railway prospered, and that if any default occurred in the monthly payments the agreement should be declared void, leaving the original claim unprejudiced. There is reason to suppose that similar, though possibly less protracted, terms have been accepted by the Japanese creditors of the Peking–Suiyuan Railway.
- 138. These settlements have reacted adversely on the Ministry of Railways, which appears to be animated solely by the desire to wipe the slate clean by any available means in order to be able to borrow again. British claimants have, however, so far refused to accept offers made by various railways for such settlement.
- 139. Unpromising as the outlook is, it is nevertheless becoming increasingly evident that the Ministry of Railways, as also other high authorities of the Chinese Government, now realise the importance of coming to some settlement of railway indebtedness, as a means to, or in conjunction with, further borrowing. Various methods of approach have been attempted.
- 140. In December 1933, discussions were begun between a representative of the Ministry of Railways and the commercial counsellor of this Legation with a view to finding ways and means for the payment of British railway loans in default. These were temporarily suspended in February, partly because the commercial counsellor left Shanghai for a tour in South China and partly because he had learned that Messrs. Monnet and Drummond, who had been engaged by Dr. T. V. Soong to come to China to report on the reconstruction work that should be undertaken, were, it was discovered, also working on a scheme for the reformation of the railways. It was accordingly thought better not to duplicate the work. On its transpiring, however, that M. Monnet's scheme for railway reorganisation appeared to aim at placing all railway creditors on an equal basis and to form only part of a much wider scheme for the redemption of the whole of the external debt of China, the commercial counsellor's exploratory discussions with the Ministry were reopened in April.
- 141. In May, however, Generalissimo Chiang Kai-shek confidentially informed His Majesty's Minister that he wished to apply to the railways a system similar to the Customs Administration, and would like to see at the head of it an eminent British expert. The proposal was known only to himself and the Minister of Finance; and it is significant that the Minister of Railways has not been informed of it. It was eventually suggested in November that General Hammond should come out for a period of four months to draw up a scheme of reform, accompanied by a trained secretary and a younger expert, to the latter of whom should afterwards be given the task of administering the scheme. This suggestion has been favourably received by the Minister of Finance, but has not yet been approved by the generalissimo. It is understood that the administrator would be under the orders of the Minister of Railways, and would be expected to submit and carry out schemes for financial and constructive reform.
- 142. Concurrently with, but quite independently of, these proposals, Mr. Calder Marshall, the chairman of the British Chamber of Commerce at Shanghai, has been discussing with the Ministry of Railways a scheme for the rehabilitation of Chinese railway finance. As, however, this scheme might

conflict with the proposals ultimately made by the British expert, if one is appointed, Mr. Calder Marshall has been induced temporarily to break off these discussions.

- 143. In September M. Monnet communicated to the representative in London of the British group in the consortium, and also to the Foreign Office, the scheme which he had tentatively drawn up before he left China in May 1934, for the rehabilitation of Chinese railways. The scheme purports to enable the railways to balance net revenues and all disbursements, including debt charges, without recourse to outside governmental help. It is proposed, however, that the Government guarantee of the service of the railway loans be implemented to the extent that $2\frac{1}{2}$ per cent. be paid on all railway debts (funded into new general bonds for each line) whether this amount is earned or not, while the return to bondholders beyond that amount would be dependent on the earning capacity of the particular line. It is suggested that interest be limited to 5 per cent. on all bonds, any surplus being paid to the Ministry of Railways' central fund, from which should be made good the guaranteed $2\frac{1}{2}$ per cent. on other lines. Material debts to be paid from operating expenses. Administrative reforms are but vaguely outlined, though recognised as essential.
- 144. Meanwhile, extensive new construction has continued throughout the year, but, unfortunately, it is largely financed from railway earnings pledged to holders of bonds in default, as well as from other more legitimate sources. Some details of the new construction at present in hand or under consideration are given in the succeeding paragraphs.
- 145. In North China work is progressing steadily on the Shansi Provincial Railway, which is planned to connect Tatung (on the Peking-Suiyuan line) in the north with Puchow (adjacent to Tungkuan, on the Lunghai line) in the south. Construction is proceeding northwards and southwards from Taiyuan, the provincial capital. The contract is believed to have been secured by a German firm, while the work is carried on under Japanese advisers. Simultaneously, work is progressing on the southward extension of the Government-owned Chengtai line from Yutzu to Tungkuan, on the Lunghai Railway. This extension runs parallel to the southward extension from Taiyuan of the provincial line from Tatung to Puchow. Progress has been made on the Lunghai Railway eastward and westward extensions. The eastern end has now been completed and now links up with the new port of Lienyunkang (Haichow), and the line was opened to traffic on the 4th October. The Taierh-chwang-Chochwang branch is nearing completion. The western extension is now open to traffic as far as Lengkow, 30 miles east of Sian. It is reported that this section will be complete and traffic opened on the 1st January, 1935.
- 146. In Western China plans are under consideration for a line from Chengtu to Chungking, and also from Chungking to Yunnan, and thence to Burma, but no steps appear yet to have been taken to put any such schemes into effect.
- 147. In Central China rails are being laid in Northern Anhui on sections of the line from Huaiyuan to Yuchikow (on the Yangtze); and in the south the Wuhu–Tunki Railway was reported to have been opened to traffic on the 1st November. Moreover, contracts with a Sino-German syndicate for the construction of a line from Yushan via Nanchang to Pinghsiang, to link up Chekiang and Kiangsi, have been concluded. Construction on the Nanchang–Yushun section started on the 21st July and is expected to be completed in eighteen months. In addition, the Wuhu–Chapoo Railway in Kiangsu is nearly complete, and work for the completion of the Shanghai–Hangchow–Ningpo Railway was begun on the 11th November, following on the signing of the loan agreement on the 8th October reported above.
- 148. In pursuance of the agreement made by the Boxer Indemnity Board of Trustees in 1933 for the completion of the Canton-Hankow Railway (see paragraph 225 of the annual report for 1933), a 6 per cent. Sterling Indemnity Loan for £1,500,000 was issued by the Ministries of Railways and Finance, and purchased by the Central Bank of China, the Bank of China, the Bank of Communications, and the Hong Kong and Shanghai Bank, on the 1st August, 1934. Construction is steadily progressing, and it is hoped to complete the line

by the end of 1936. The extension northwards from Shiuchow to Lokchang was opened to traffic on the 1st February, and a trial service was operated on the new section between Leibokow and Tsuchiayen on the 10th October. No progress has been made with regard to the old project for a loop line to connect the Canton–Kowloon Railway with the Canton–Hankow Railway, and the question was not raised during the negotiations for a new working agreement between the British and Chinese sections of the line. In the neighbourhood of Canton, however, survey of a line from Samshui–Hohsien, linking Kwangtung with Southern Kuangsi, was completed in May.

IV.—SHIPPING.

- 149. Shortly after the National Shipping Conference held at Nanking in March, the proceedings of which were not published, it was announced in the press that the Shanghai Chinese Shipping Association had appointed a committee to devise ways and means of securing closer co-operation among Chinese shipping companies with a view to the retrocession of the navigation rights of foreign companies.
- 150. In August the Navigation Bureau at Shanghai refused to issue to a British vessel a survey certificate (see paragraph 231 of the annual report 1933), and the vessel was consequently unable to obtain an inland water pass. In refusing, the bureau stated that the Ministry of Communications had ordered that, pending the submission and approval of the association's report on co-operation, no fresh vessels were to be allowed on any shipping route. The Legation made strong representations to the Chinese Government on treaty and general grounds, and were informed in November that the report on co-operation having been received, the placing of additional vessels on inland water routes was again permitted.
- 151. In September 1933 the Hankow Navigation Bureau informed the local British shipping companies that the bureau had set up a Collision Arbitration Commission to deal with all cases in connexion with disputes arising from collisions. A dispute in which a British ship was involved in a collision at Kiukiang in March was, however, not brought before the commission. In September 1934 regulations were published in the press governing a new Commission for the Settlement of Maritime Disputes, to be established under the Navigation Department of the Ministry of Communications, but these have not yet been put into effect.
- 152. In January the Hankow Bureau requested British shipping companies to supply details regarding their ships crews "for the purpose of improving the treatment of employees and reducing the number of men with inadequate qualifications." The Chinese Government requested the bureau to discontinue these activities. The bureau in July renewed the request for these particulars; the request was ignored, and no more has been heard of the matter.
- 153. In May the Hankow Navigation Bureau refused to accept Lloyd's certificates as sufficient for the issue of Inland Water Certificates. Representations were, however, made to the Ministry for Foreign Affairs, and the Ministry of Communications issued an order in August that, "pending recovery by negotiation of inland water navigation rights, survey and measurement certificates held by all foreign vessels which are issued by a Lloyd's surveyor, or by the competent authority of the vessel's nationality, should for the time being be accepted."
- 154. In September 1933 the customs notified the public that the Chinese Government had issued towage regulations providing—
 - (1) That all towed vessels must apply to the Ministry of Communications, direct or through the local Navigation Bureau, for registration and issue of a permit to be towed;

(2) No towed vessels would be cleared by the customs without production of the permit; and

(3) That the measurement and inspection of such vessels would be undertaken by the Navigation Bureaux. 0

Foreign vessels were at first exempted from applying for permits to be towed, though they were required to obtain survey and inspection certificates from the bureau. In April, however, on instructions from the Nanking Government, foreign firms were informed by the Customs that the regulations would be applied in their entirety to foreign as well as to Chinese vessels as from the 1st June, 1934. As all passenger boats and foreign-type cargo boats towed by launches running under the Inland Steam Navigation Regulations were already required to register with the Customs and to obtain a permit to be towed, the regulations in so far as such towed vessels were concerned merely transferred these functions to the Navigation Bureaux. The new regulations, however, applied equally to vessels towed by river pass vessels which had not hitherto required permits to be towed, and in respect of which His Majesty's Government in the United Kingdom do not admit the competence of the Navigation Bureaux. It was accordingly felt that to concede the right of the Customs to refuse clearance to such towed vessels, except on production of permits to be towed issued by the Navigation Bureaux, would be to accept a breach of our treaty rights and weaken our defence against the efforts of the bureaux to abstract all control of shipping from the Customs. Instructions were accordingly issued to consuls to draw a distinction between vessels trading under Inland Steam Navigation Regulations on the one hand, and coastal and river pass shipping on the other, and British firms were informed that there was no objection to compliance with the requirements of the bureaux as regards towage under the above regulations. At the same time, the Ministry for Foreign Affairs were reminded of our attitude towards the bureaux (see paragraph 231 of annual report 1933), which had in no way been modified by our acquiescence in the extension of their control to towed vessels registered for inland water trade. In May the Navigation Bureaux at Shanghai and other ports issued a notice that the regulations would be enforced as from the 1st June on all towed lighters of whatever nationality. Most British lighters towed by river pass steamers also run under Inland Steam Navigation Regulations and are consequently, in any case, provided with Navigation Bureaux permits to be towed, but a small number do not. The shipping companies decided that they would in no circumstances take out permits to be towed for lighters exclusively towed by river pass vessels, or produce permits to be towed in respect of lighters holding such permits for use under Inland Steam Navigation Regulations when such lighters were towed by river pass vessels, and, as it was anticipated that the Customs would in these circumstances refuse clearance to river pass steamers towing lighters, a critical situation threatened to arise. Sailings were suspended by the shipping companies and renewed representations were made to the Nanking authorities. His Majesty's consul-general at Shanghai was informed by his Japanese colleague that his Government intended to ignore the requirements of the Navigation Bureaux entirely, both as regards inland and other shipping, and would, if necessary, use force to protect Japanese vessels from interference. On the 15th June the Inspector-General of Customs informed His Majesty's consul-general at Shanghai that the towage regulations had been temporarily suspended for foreign flag tows. Nothing more has been heard of the matter, but in the event of any renewed attempt to force on British coastal and river vessels regulations such as those in question instructions have been received from the Foreign Office "to inform the Chinese Government in the firmest possible language that, until the existing treaties are altered by mutual agreement, British vessels will not submit—any more than British subjects—to any form of extra-treaty Chinese control."

- 155. On the 28th April the *Ministry of Communications Gazette* published regulations governing the registration and licensing of wharf-boats, the effect of which was to place under the control of the Navigation Bureaux all hulks and pontoons used for mooring steamers, embarking and disembarking passengers, and loading and unloading cargo. No attempt has been made to enforce these.
- 156. A Navigation Marks Ordinance promulgated in May places the control of navigation marks, including lighthouses, under the control of the Navigation Bureaux, instead of as hitherto under the Customs. It has, however, not so far been put into force.
- 157. In connexion with schemes for the reorganisation of the China Merchants' Steam Navigation Company, now owned by the Chinese Government,

tentative discussions took place in April with the Minister of Communications of a proposal made by him that a working agreement might be effected with the British shipping companies whereby the latter provided the necessary capital and administered the shipping operations. The company lacked expert administration and was loaded down with debt; it had been working on an overdraft which cost them 1 per cent. a month, and this could not go on; some 15 million dollars was required for reorganisation.

- 158. The first of four coasting ships built in England with the proceeds of the loan made by the Board of Trustees of the Boxer Indemnity Fund in August 1933 arrived in Shanghai on the 31st October, and two new river steamers are being constructed at Shanghai.
- 159. In pursuance of a resolution passed by the 16th National (i.e., Domestic) Through Transportation Conference held at Nanking in September 1933, arrangements were made early in 1934, under the direction of the Ministry of Communications, by which through bills of lading might be issued by all Chinese Government railways, at any rail centre, covering transport over the railway and carriage by China Merchants' Steam Navigation Company's steamers to the port of destination (and vice versa). All other Chinese steamship companies of repute have subsequently been included, and agreements with a number of railways have been made. Application for similar facilities made in August by Butterfield and Swire was rejected. The Legation has protested that such refusal is contrary to article 5 of the Nine-Power Treaty. The question is at present only of practical importance in connexion with Lienyun-Kang (the new port at Haichow—see under Lung-Hai Railway), but is potentially very serious.
- 160. As a result of the dispute, settled at the end of 1933, between the Canton Seamen's Union and Messrs. Butterfield and Swire, the local Canton importers' guild, through their representatives at northern ports, boycotted the company's ships with a view to extracting large sums claimed by the guild for indirect losses due to the strike. The dispute was settled and the boycott lifted in July by the payment by the company to the chairman of the Canton Merchants' Association at Shanghai of 115,000 dollars in cash and of a deferred cheque for 115,000 dollars cashable after the company were satisfied that the guilds had adhered to the agreement. Further trouble between the Canton Seamen's Union and Messrs. Butterfield and Swire threatened in July, over the non-registration with the union of certain northern seamen in one of the company's ships, but came to nothing.
- 161. A strike threatened by the Canton Seamen's Union against the Canton and Macao Steamboat Company (Limited), in April on behalf of a British master dismissed for incompetence, who had joined the union, resulted in an attempt to blackmail the company for 10,000 dollars and payment of the master's passage back again to London. Only the personal intervention with the high provincial authorities of the consul-general and the British Commander-in-chief (who happened to be in port) prevented the strike being made effective.
- 162. In April the Swatow branch of the Canton Seamen's Union engineered a strike of the crews of two ships of the Douglas Steamship Company, as a result of which the company's recruiting agent in Hong Kong agreed not to interfere with the union by introducing his own men for engagement by the company, the company accepted a warning that the guarantee (against smuggling) system was not recognised by the union, and the company paid the union 2,000 dollars for mythical "losses."
- 163. The Canton Seamen's Union has made persistent endeavours to obtain permission to establish a branch in Hong Kong, which the colonial authorities have categorically refused.
- 164. At the end of December 1933 the National Opium-Suppression Committee instructed the Kiangsu and Anhui Provincial Governments that no opium-suppression agents were to board foreign vessels plying on the Yangtze. No complaints have been received in regard to any such searches.
- 165. At Wuchow irregularities in connexion with armed parties, acting on behalf of the provincial tax bureau, boarding Hong Kong Chinese-owned British ships were amicably adjusted as the result of discussions between the local

authorities and the acting consul (deputed from Canton for the purpose), who was accompanied by the captain of a British gunboat on the West River.

- 166. At Swatow an impracticable and obnoxious scheme for boarding incoming vessels and searching the passengers was eventually dropped, partly owing to the intervention of His Majesty's consul-general at Canton with the high provincial authorities, and partly probably to the appearance in port of a British man-of-war. (For preventive measures and smuggling, see under Customs.)
- 167. In January a party of fifty armed Chinese soldiers came aboard a British ship at Foochow and demanded free passage to Amoy. They were persuaded to hand over their arms to the chief officer, and were eventually ejected by an armed party from H.M.S. Wild Swan.
- 168. At the request of British shipping companies, His Majesty's consulgeneral at Shanghai has agreed to treat Yangtze river steamers as "home trade passenger ship," so permitting a reduction in the number of certificated officers carried. The companies are also pressing for wider acceptance of Chinese officers, and His Majesty's consul-general has, in this connexion, expressed the opinion that we should be justified in accepting certificates of competency issued by Chinese Government Departments since the beginning of 1934. The Chinese Government has already, through the Inspector-General for Foreign Affairs at Canton, requested that such certificates should be accepted for the Chinese captains of Chinese merchant vessels visiting Hong Kong, including the four recently purchased from British Boxer Indemnity funds; the matter has been referred by the Hong Kong Government to the Colonial Office for instructions.
- 169. In connexion with the Safety of Life at Sea Convention, 1929, to which China acceded in February 1933, the British shipping companies have expressed the opinion that it would be extremely dangerous to ask the Chinese Government to be responsible for the issue of convention certificates to British ships trading in Chinese waters, and that the survey of such ships not calling at Hong Kong should be undertaken by His Majesty's Government's marine surveyor in Shanghai. With regard to the "Memorandum relating to the Carriage of Dangerous Goods and Explosives in Ships," the Chinese Government agrees, except that it considers the restrictions imposed on the carriage of Chinese crackers (fireworks) should be relaxed.
- 170. As the result of the identic communications regarding the new Pilotage Regulations addressed by the foreign consuls at Shanghai to the Inspector-General of Customs and the Mayor of Greater Shanghai (see paragraphs 232–236 of annual report, 1933), and of similar representations made by the Inspector-General to the Ministry of Finance, and by the British, French and American Legations to the Ministry for Foreign Affairs, the Chinese Government in May stated that the assets of the Shanghai Pilots' Association would be paid for and taken over by the Customs, which would meet all retiring payments, &c., due to the pilots, that pilots now serving would carry on as before, that pilots taken on in future would be men of experience duly examined, and that all matters connected with inland water and coastal pilotage would be placed in control of the Customs. As these assurances were not sufficiently precise. His Majesty's Minister made further representations and was assured in reply that the new provisional regulations would be revised. Revised regulations, which, in general, met our requirements, were communicated by the inspector-general to the consuls at Shanghai in June, though no mention was made of arrangements for taking over the assets of the existing Pilots' Association. His Majesty's consulgeneral was authorised to negotiate on the following points: namely, recruiting of pilots other than Chinese; discretion to retain pilots over age; experience in handling ocean vessels as a qualification for apprentice pilots; no exemption from compulsory pilotage of Chinese Government merchant ships; reservation of treaty rights regarding compulsory pilotage, and prior conclusion of arrangements for taking over existing equipment, &c., before acceptance of the new regulations. Proposals satisfactory to the present pilots for taking over the assets, &c., of the Pilots' Association have been unofficially communicated, and our wishes regarding the other points have been met. The attitude of the Japanese, who have consistently been opposed to alteration of the existing system, still remains

uncertain though it now appears that they might be prepared to agree to the regulations as now revised provided arrangements could be made whereby the proportion of foreign pilots should be in accordance with the amount of pilotage fees paid by the shipping of the respective nationalities, and provided that Japanese ships used Japanese pilots. The negotiations being conducted at Shanghai have included arrangements for other ports.

V.—MINING.

- 171. At present the affairs of the three British mining enterprises appear to be progressing satisfactorily.
- 172. With regard to the Mentoukou Coal Mining Company near Peking, a predominantly Chinese Sino-British partnership, there is little to record beyond the fact that they are being pressed to register under the Chinese Company and Mining Laws and are considering doing so. They have come to terms, though no agreement has yet been signed, regarding the settlement of a long outstanding claim against the Peking–Suiyuan Railway in respect of a branch line on which their coal is transported. There have been no labour disputes, and none of the usual trouble in connexion with underground encroachments by contiguous native-owned pits. In May the Ministry of Industries issued them new mining area licences, notwithstanding the non-settlement of a dispute as to boundaries with the native Hsieh Cheng Company.
- The Peking Syndicate, operating since last year as partner with the Native Chung Yuan Company in the Chinese amalgamation known as the Chung Fu Administration, has, as for many years past, suffered vicissitudes which have given rise to alternating despair and comparative optimism. The year opened with rioting at the mines which threatened the lives of British residents, and the syndicate's local representative was withdrawn. Briefly, the position was that General Liu Shih, a subordinate of Generalissimo Chiang Kai-shek, had either insufficient forces or was unwilling to use force to control rival native interests: the various Chinese interests both in the Chung Yuan Company and in the Chung Fu Administration were intriguing against each other: the principles of the amalgamation agreement were ignored by the Chinese partners who persisted in the uneconomical working of their own pit with the result that the loan of 2,300,000 dollars made by the syndicate's subsidiary, the Anglo-Chinese Finance and Trade Corporation against old stocks at the mines was not being paid off: the Tao Ching Railway was forced, or possibly preferred, to allocate freight to the native pits, so that the old stocks pledged to the syndicate could not be transported for sale: the native pits outside the administration's area, in which, however, the Chinese members of the administration were personally interested, continued to operate at prices against which the administration could not compete; owing to overstaffing and bad management the operating expenses of the administration were enormous; the net result was that the administration was working at a loss of some 200,000 dollars a month, payments were not being made in respect of the loan from Anglo-Chinese Finance and Trade Corporation, and the administration had by February this year incurred liabilities for wages, freight, &c., amounting to some 500,000 dollars. The position was that no true amalgamation had ever taken place, and that owing to the power of native local vested interests the syndicate was powerless. So serious was the position that early in February Major Nathan requested the Chinese Government to appoint receivers to wind up the administration. The Ministries concerned stated that the loan from the Anglo-Chinese Finance and Trade Corporation never having been submitted for approval, the steps taken by the joint administration had been irregular, but that as measures were being concerted for drastic reorganisation the liquidation of the administration was unnecessary.
- 174. During his visit to Nanchang in May His Majesty's Minister made strong personal representations to Generalissimo Chang Kai-shek. The latter immediately sent a strongly worded telegram to his subordinate, General Liu Shih, the Military Governor of Honan, which he has since followed up with further peremptory orders. As a result of this action in September the Chinese directors of the Chung Fu Administration and the Chung Yuan Company, as

also the general manager and assistant manager, had been dismissed, while the commander of the local gendarmerie and four officers were to be court-martialled, and the "principal villain of the piece," the chairman of the Chung Yuan Company and concurrently Honan Commissioner of Finance, was under notice to proceed to Nanchang for "examination." The generalissimo has also appointed a direct personal representative as local Commissioner of Reconstruction, and has placed 1,500 troops at the mines to see that these drastic orders are obeyed. In short, the personal intervention of His Majesty's Minister with the generalissimo has apparently resulted in the immediate and complete elimination of that effective opposition from local vested interests which has been one of the principal factors in preventing the successful conduct of the syndicate's affairs. It remains to be seen how far these desirable conditions can be maintained.

175. The affairs of the Kailan Mining Administration have also given rise to great anxiety. During the first three months of the year there were serious and recurrent labour troubles in the mines area, which is, of course, situated in the "demilitarised zone" wherein no regular Chinese forces are allowed to be stationed. These troubles were the result of political and economic factors which remain obscure and were aggravated by the inadequacy of the local Chinese police and the lack of military force to overawe the disaffected elements. At the request of the Kailan Mining Administration an investigation on the spot was made in April by the Acting Chinese Secretary, accompanied by a military language officer, as a result of which it was decided that no useful purpose would be served by the despatch of British forces to the mines area. Representations, however, were made to the Hopei provincial authorities for the strengthening of the police. Although owing to difficulties with the Japanese this has not yet been effected, no further troubles have been recorded up to the end of the year.

176. In April the general manager of the Kailan Mining Administration and representative in China of the Chinese Engineering and Mining Company (Limited), as the result of negotiations continued since July 1933, came to terms for the revision of the Amalgamation Agreements of 1912 and for the issue of a mining permit under the Chinese Mining Regulations. The Chinese Engineering and Mining Company offered, and its Chinese partner, the Lanchow Mining Company (Limited), accepted, an arrangement whereby the interest in and ownership of the assets of the Kailan Mining Administration, as well as the duties and responsibilities for its management, would be equally shared by the two companies: a joint petition signed by both companies was presented to, and approved by, the Ministry of Industries applying for the grant of the whole mining area to the Kailan Mining Administration as reconstituted; and a sum of 1 million dollars was advanced by the Chinese Engineering and Mining Company on behalf of both companies in respect of mining royalties payable to the Chinese Government. On the 10th August an agreement was duly signed between the Chinese Engineering and Mining Company and the Lanchow Mining Company on the above lines, providing for the operation of the reorganised joint administration in accordance with the Chinese Mining Law and for the equal participation of the two partners in the profits, management, and ownership, of the mining rights and properties. Copies of this agreement have been officially communicated to His Majesty's Legation by the Ministry for Foreign Affairs. Questions have now arisen as to the manner in which the properties of the Chinese Engineering and Mining Company shall be transferred to the joint ownership of the administration, and as to the desirability of registration under Chinese Law of the Chinese Engineering and Mining Company as a foreign company operating in China. The Ministry of Industries has now informally raised the question of the prior registration under the Chinese Company Law of the Chinese Engineering and Mining Company before issue of the mining permit jointly to the partners in the administration.

VI.—FINANCE AND TAXATION.

Finance.

177. Information was received in June that, whereas the monthly revenues of the National Government amount to some 18 million dollars, monthly expenditure, owing mainly to the increased demands of the military, had risen to some

30 million dollars, and that for many months there had been a deficit of 10 million dollars which, however, the Ministry of Finance had been able to meet with the assistance of funds from the Italian Indemnity Loan. A first version of the budget published in July for the 23rd fiscal year, 1st July, 1934—30th June, 1935, showed revenue 815,915,000 dollars and expenditure 915,685,457 dollars, of which roughly 450 million dollars was for the account of the military. These original estimates were hastily withdrawn, as it was considered that to show a deficit of 100 million dollars might have a damaging effect on the Government's credit and borrowing powers, and a statement subsequently appeared in the semi-official Kuomin News on the 20th July showing revenue and expenditure balanced at 777,302,226 dollars. In October, however, the Central Political Council approved a further revised version which is balanced at 918,111,034 dollars, of which 333 million dollars is for military expenditure. Payments and defaults on railway loans are left out of the reckoning, as also are the revenues and expenditure of Government Departments other than the Ministry of Finance. The accuracy of the estimates of some of the more important items of revenue is open to doubt. It seems probable that customs revenue estimated at 366,413,791 dollars will, in view of continuing trade depression, approximate more nearly to 300 million dollars. Moreover, it seems improbable that the sum of 257,530,231 dollars set aside for loan service will be sufficient to meet all the charges under this head.

- 178. As early as May the Minister of Finance was engaged in seeking any unpledged surplus or revenue which might be used as security for further loans.
- 179. A very confidential statement received from the customs shows that, whereas in the calendar year 1933 a balance of 69 million dollars from customs revenues was remitted to the Minister of Finance, the available balance for the calendar year 1934 is unlikely to exceed 43 million dollars; this sum includes 14 million dollars from the 5 per cent. revenue surtax which is unpledged. This surtax should have terminated on the 30th June but has been continued until the 30th June, 1935.
- 180. With regard to present indebtedness, loans secured on the customs have continued to be punctually met, while the railway loans and other obligations of the Government remain heavily in default. In October the Minister of Finance announced that a sum of £250,000 plus interest had been remitted to London by the Chief Inspectorate of Salt Revenue to pay the 1934 instalment of principal of the Anglo-French $4\frac{1}{2}$ per Cent. Loan of 1908, thus wiping out all arrears due to the bondholders.
- 181. With regard to the Cotton-Wheat Loan, which he had negotiated as Minister of Finance in 1933, Dr. T. V. Soong made a statement in March from which it appeared that the loan, owing to difficulty in disposing of the cotton, had been reduced from 50 million to 20 million U.S. gold dollars. In answer to allegations that the loan had been used to finance the purchase of munitions, the Minister of Finance stated in September that the entire loan had been entrusted to the National Economic Council and used exclusively for purposes of national reconstruction.
- 182. On the 12th January a new loan of 100 million dollars, known as the 23rd Year Customs Treasury Notes, was authorised. The loan is for 6 per cent. per annum, issued at 98, secured on customs revenues, to be paid off by the end of 1940, and is used to repay the Government's indebtedness to the Central Bank of China and other Chinese banks. Whereas the similar issue made last year threw a burden on customs revenues of 1 million dollars a month, the new loan will require payments from customs revenues of $1\frac{1}{2}$ million dollars a month. In November it was announced that the China Development Finance Corporation had, in conjunction with Chinese banks, purchased at a discount from the Ministry of Finance 30 million dollars of revenue stamps, thus mortgaging future revenues from that source. There has been no other borrowing by the Government for revenue purposes, but the Inspector-General of Customs while in London on furlough in October and November has been endeavouring to negotiate a longterm customs loan, in which Chinese banks would participate, in order to pay off existing obligations of the Chinese Government. It is probable that similar efforts have been or will be made in America.

183. Efforts made by the Canton authorities early in the year to raise from British banks in Hong Kong a loan on customs revenues for currency reform proved abortive.

184. Consequent on his unsuccessful attempt to create an International Corporation, Dr. T. V. Soong, then Minister of Finance, engaged M. Monnet, formerly connected with the League of Nations, to visit China to study the question of raising money for reconstruction purposes (see also section on Railways). As a result of his endeavour the China Development Finance Corporation was eventually formed on the 31st May, with a capital of 10 million dollars subscribed by seventeen Chinese banks, including the Central Bank of China, and by a number of individual prominent bankers and politicians, including Dr. T. V. Soong and Dr. H. H. Kung, the former and the present Ministers of Finance. The function of the corporation is to be that of providing the machinery by which Chinese and foreign capital could work in co-operation to finance the economic development of China, and of conducting expert examinations of projects requiring capital. Mr. T. L. Soong, brother of Dr. T. V. Soong, has been appointed general manager. The corporation is favourably regarded by the principal British interests in China concerned in undertaking such projects. Strong opposition has been evinced by the Japanese, who regard with suspicion, not only Dr. T. V. Soong, but also M. Monnet owing to his former connexion with the League, and also feel that the corporation may be used to exclude Japan from participation in the financial reconstruction of China. With regard to possible conflict with the interests of the consortium it appears that M. Monnet has expressed to the British representative of the group banks concurrence in the view that the only practical means of approach to the international money market is through the consortium which is indispensable for the purpose, though the consortium is not directly concerned with loans or advances made in China. Adherence to this attitude may tend to obviate Japanese opposition to the corporation, though the Japanese are apparently inclined to approach the problem of the rehabilitation of China from the angle of the consolidation of her total foreign indebtedness before any new loans are made, whereas M. Monnet, in agreement with the British Group, appears to favour an approach to the major problem through the settlement first of China railway indebtedness. Meanwhile, the corporation has participated with the British and Chinese Corporation in the loan for the completion of the Shanghai-Hangchow-Ningpo Railway (see section on Railways), and has advanced, in conjunction with its constituent banks, to the Ministry of Finance a sum of 30 million dollars.

185. The steady appreciation in terms of foreign currencies since 1931 of the Chinese dollar, which has reacted to the detriment of her export trade, combined with a heavy falling-off in remittances from Chinese abroad and absence of foreign investment in China, have led to an adverse balance of payments which, in the absence of sufficient stocks of gold, can only be met by exports of silver.

Moreover, though there was a continued rise in the exchange value of the Chinese dollar as a result of the introduction of the United States silver buying policy in May, Shanghai exchange, owing to China's unfavourable balance of payment, to lack of confidence in the Chinese dollar, and to fears of an embargo on the export of silver, did not rise to parity with silver abroad and it was consequently profitable to export silver. Whereas in the whole of 1933 only approximately 70 million dollars were exported, during the six months March to August 1934 nearly 160 million dollars were exported of which half were shipped in August. Shipments were mainly effected by the foreign banks in Shanghai, all of whom held large stocks, partly money remitted for safety from the interior and partly money for financing imports. Speculators' contracts are inextricably interwoven with genuine trading transactions. On the 9th September, partly in order to prevent exchange fluctuations due to the activities of speculators and partly to make the export of silver unprofitable, the Ministry of Finance prohibited purchases or sales of foreign exchange except for normal business requirements. The outflow of silver, however, continued and on the 15th October the Chinese Government, without warning, imposed customs duty on exports of silver as follows: On silver dollars and mint bars, 10 per cent., less $2\frac{1}{4}$ per cent. minting charges paid, i.e., $7\frac{3}{4}$ per cent. net; on other forms of silver, 10 per cent. (in lieu of 24 per cent.); in addition, an equalisation charge on exports of silver

equal to the deficiency, if any, existing between the theoretical parity of London silver and a rate of exchange officially fixed by the Central Bank of China, after making allowance for the export duty.

187. As the silver exported formed only a small proportion of the large stocks which had long been lying idle in the banks, it is doubtful whether exports had endangered the currency situation, and it is possible the Government may have been actuated partly by the wish to take from the foreign banks the initiative in fixing exchange rates while at the same time giving the Central Bank of China the profitable monopoly of export.

188. Apart from holding up large shipments of silver for which the Customs had issued permits to export, the immediate effect of the new duty, which, as at first imposed, acted as a complete embargo, was a heavy drop in exchange, followed by temporary chaos. A Stabilisation Committee was, however, set up, and the procedure was shortly modified to enable bankers to adjust differences by the export of silver if necessary, with the result that exchange has become more stable. Silver, however, is still disappearing by smuggling and hoarding, and this would increase dangerously were a rise in the world price of silver greatly to increase the present disparity with local rates of exchange. In that event it might be necessary to abandon the attempt to maintain stability of exchange, or to face a depreciated currency.

Taxation.

189. Drastic revision of the rates of consolidated tax on rolled tobacco, with a view to increasing the revenue and to reducing the incidence of the tax on small native manufacturers, has been under consideration and caused grave concern to the British American Tobacco Company and other foreign manufacturers of cigarettes. The matter has apparently been adjusted by the introduction of one new rate which is unobjectionable from the foreign manufacturers' point of view, and by the purchase of 30 million dollars worth of revenue stamps by the China Development Finance Corporation.

190. The business tax has continued to give rise to much concern. Hankow the export business tax, as an additional levy on the local export trade, continues to be levied and has now been extended to bast fibres, egg products, sesamum, and casings, in addition to wood oil, tea, hides and skins; no attempt has yet been made to enforce the business tax proper there. At Canton the tax imposed on kerosene though referred to as a "business tax" was in reality a tax on goods similar to the export business tax at Hankow. As regards the business tax proper the Kwangtung Provincial Department of Finance has endeavoured to extend its collection to foreign firms both in the native city and on Shameen, and in May the mayor once more requested the consuls to instruct their nationals to pay the tax. In August the Chinese Chamber of Commerce at Canton invited foreign firms to meet them for discussion of the question; this meeting was ill attended and in October the chamber addressed a circular letter to foreign firms threatening them with a boycott, unless they paid the tax. The chairman of the Provincial Government, however, has now assured His Majesty's Minister that no high-handed measures will be taken, and agreed that the matter be treated as a national question. At Kiukiang demands were in November made on the foreign shipping companies to pay the tax. The business tax was one of the major questions under consideration at the National Finance Conference held at Nanking in May, when a resolution was passed that the Ministry of Finance be requested to decide on measures to improve the system and that the Ministry for Foreign Affairs be requested to proceed with negotiations for application of the tax to foreign firms. In pursuance of this resolution the Ministry of Finance in June formulated a set of measures for readjustment of the tax, and the Ministry for Foreign Affairs in October addressed a note to the foreign representatives requesting that their nationals be instructed to pay the tax in accordance with the regulations. This communication, which is now under consideration, fails satisfactorily to answer the main objections which we have made to the tax in the past. The question is regarded as one of the utmost gravity by British firms, and the policy of His Majesty's Government in the United Kingdom in relation to the tax has given rise to adverse criticism,

- 191. Amongst over 100 resolutions adopted by the second National Finance Conference held at Nanking in May, the following were the most important: (i) Reduction of farm taxation; (ii) abolition of exorbitant taxes and miscellaneous levies before the end of 1934; (iii) reform of the tax system; (iv) definition and demarcation of provincial and district revenues and expenditure; (v) the introduction of measures to develop economic productivity; and (vi) the reservation as subsidies to the Provincial Governments of part of the revenue accruing to the Central Government from the stamp tax, while, at the same time, allowing the whole of the wine and tobacco licence tax to be collected by the local authorities. A semi-official statement published by the Nanking Kuomin News Agency on the 11th October claims that substantial progress has been made in a number of provinces towards putting these resolutions into effect. In particular, with regard to exorbitant levies and miscellaneous taxes, by which British commercial interests are directly affected, it is claimed that these have already been abolished to the extent of 9½ million dollars, and that the Province of Kwangtung is responsible for more than half this sum. All such levies, to the extent of 1,600,000 dollars, have, it appears, been abolished in Hunan. No steps have apparently been taken in Shansi, Shensi, Honan, Ninghia, Kansu, Kiangsi and Yunnan. The amounts abolished in Chekiang, Anhui, Hupeh, Fukien and Shantung are insignificant. In each of the provinces, Hopei, Chahar and Kwangsi, about 500,000 dollars of such taxation are stated to have been abolished.
- 192. With regard to the subsidy to the provinces from the stamp tax, it should be recorded that the Government attempted to cancel at extremely short notice all revenue stamps already issued, but was eventually induced by the universal outcry which this proposal invoked to allow a reasonable period within which stamps of the old issue might be used up before replacement by the new.
- 193. In June also the Ministry for Foreign Affairs circulated to the foreign representatives a statement that an order issued in 1928 prohibiting the flotation of loans by organs of the Central Government or by the provincial authorities without the approval of the Central Political Council had been reaffirmed, and added that such unauthorised loans would be regarded as invalid. A number of provincial loans have in fact been submitted for approval, but in two important instances the Canton authorities have ignored the order (see Oil Taxation below, and the Kwangtung Iron and Steel Works under the section on Trade).
- 194. In June the Central Government issued a special mandate prohibiting levies on goods on which the consolidated tax has already been collected by the Central Government.
- 195. Complaints have been received from British firms in the course of the year regarding "illegal" taxation in Foochow, Amoy, Szechuan, Swatow, Hunan and other places, on oil, soda ash, artificial fertilisers, and other goods. The following notes on major taxation questions in respect of which the intervention of the Legation has been invoked make it clear that though through a system of subsidies some progress may have been made towards the centralisation of internal taxation, the provinces, especially Kwangtung, retain a very large measure of fiscal autonomy in matters of taxation.
- 196. The settlement of the difficulties experienced by the foreign oil companies in importing crude oil into Kwangtung for refining purposes and the proposal of the local authorities to impose a "business" tax on retailers of 3 dollars a case on both imported and locally refined oil were reported in paragraph 249 of the annual report for 1933. Early this year, however, the authorities proceeded to refund to the native distillers two-thirds of this tax. There remained, moreover, the objection that the tax was also applied to imported kerosene, and was in effect a tax on goods contrary to the assurances given to the oil companies by the Minister of Finance in 1931 and also to the spirit of the tariff treaties. Both with regard to this tax, and to a similar tax of 1 dollar a unit in Fukien, repeated instructions for cancellation issued by the Ministry of Finance at Nanking have been ignored by the local authorities. All representations to the Provincial and National Governments having failed to remedy the situation, the Asiatic Petroleum Company and the two American oil companies entered into direct negotiations with the Canton Government, as a result of which an agreement was signed with the Provincial Finance Department on the

28th September. By this agreement the companies secretly advanced 5 million dollars to the Provincial Government, and the latter revised the regulations so that 87 dollars is now levied on each ton of kerosene distillate imported; the foreign companies will obtain a receipt for this sum, but will actually only pay 29 dollars, the balance of 58 dollars being credited against the advance; the native importers will pay the full 87 dollars. The companies hope to reimburse themselves in fourteen months, or less. Great secrecy was maintained, but rumours of the advance reached Nanking, and informal protests, on the grounds that unauthorised provincial loans are prohibited, have been made by the Vice-Minister for Foreign Affairs and by the Ministry of Finance to the British and American representatives at Nanking. We have admitted that such an agreement exists, but have declined, on the grounds that it was communicated confidentially from private sources, to supply Nanking with a copy.

- 197. Orders have been issued by the Inspector-General of Customs to the Commissioner of Customs at Canton that fuel oil containing 99 per cent. kerosene, which includes kerosene distillate, is to pay full kerosene duty of 1·43 gold units per 10 American gallons (in case) or ·35 gold units per 10 litres in bulk, instead of 2·90 gold units per ton, the import duty hitherto levied at Canton. The South-West Political Council have given instructions that the inspector-general's new order is not to be enforced.
- 198. In November the Kwangtung Provincial Government imposed an additional levy of 20 per cent. ad valorem on rolled tobacco, contrary to the national regulations governing the consolidated tax. The Central Government under present arrangements already refunds to the cigarette companies the amount of the consolidated tax collected in Kwangtung which has already been paid at source by the companies to the Nanking authorities, and the Central Government is now called upon to refund also the amount paid in respect of the new 20 per cent. ad valorem levy. According to semi-official Kuomin reports the Central Government has made strong representations which the Provincial authorities have apparently ignored. The intervention of His Majesty's Legation has not been requested and the British American Tobacco Company, in conjunction with the Chinese manufacturers at Shanghai, and with the support of the Tax Administration, are withholding supplies and adopting other measures to fight the tax.
- 199. A tax on imported foreign agricultural products was imposed by the Canton authorities in July as a measure of protection of native produce. It was felt that in view of the virtual independence of the province it would serve no useful purpose to ask Nanking for an explanation of this local extra-customs levy, at variance with the financial policy of the Chinese Government and with the assurances given in 1928 at the time of the Tariff Treaty.
- 200. Protective taxes instituted in Kwangtung and Shansi for native provincial industries, discriminating not only against foreign goods, but also against imports from other provinces, are referred to under Trade.

VII.—TRADE.

201. The customs revenue figures for the first ten months of the year are:—

				Dollars.
Imports	Jan J.	BERL TO	inores la	874,114,029
Exports	COLLEGE STATE			441,865,850
	Total			1 315 070 970

These, as compared with the same period in 1933, show a falling off of 283,809,861 dollars, or 24 per cent., in imports, and of 65,088,839 dollars, or 12·8 per cent., in exports, and a total decrease of 348,898,700 dollars, or 21 per cent., in the total volume of trade. This is probably to be attributed mainly to a diminished purchasing power both in China and in the countries with which she trades, though increased import duties and smuggling are also responsible to a degree which it is impossible to assess.

202. At the end of October the excess of imports over exports totalled 432,248,179 dollars as compared with 650,969,201 dollars for the same period in 1933. It is considered that the total unfavourable balance of trade for 1934 will amount to approximately 500 million dollars as against 733,739,198 dollars in 1933. The principal decreases have been in imports of cotton piece-goods, 29.6 million dollars; cereals and flour, 157.8 million dollars; and candles, soaps, oils and fats, 65.2 million dollars; and in exports of textile fibres, 34.65 million dollars; exports of piece-goods, 15.56 million dollars. There has been an increase of approximately 15 million dollars in imports of machinery. Invisible exports, principally in the form of remittances from overseas and of foreign capital investments in China, have continued to decrease.

203. The United States, Japan and the United Kingdom have supplied a larger percentage of imports than last year.

204. Much attention has been paid to the necessity for adjusting the adverse trade balance by fostering native industries and exports, and by obviating the necessity of importing much that might be produced in China. These measures, as detailed below, have sometimes been both inexpedient and discriminatory against foreign vested interests, and have sometimes been obscured by the desire to secure credit for enterprises in themselves ill-considered, but some positive steps have been taken towards a much needed and radical economic reconstruction of agricultural, commercial and industrial conditions.

205. Reduction in export duties on agricultural produce and certain native manufactures is referred to in the section on Customs.

206. In September 1933 the Minister of Industries announced an elaborate national Four-Year Industrial Plan, which was divided into three sections: economics; manufacturing and mining; and agriculture and forestation. It was apparently, in practice, to be confined, meanwhile, to the Yangtze Valley. In principle heavy industries were to be operated by the State, while light industries would be left to private enterprise. A policy of controlled production of established industries and the creation of "medium scale" new industries is advocated. The various goods covered by the scheme are necessaries, e.g., coal, iron and steel, copper, petroleum, acids, machinery, automobiles, sugar, paper, porcelain, rice, wheat, flour, raw cotton, piece-goods, fruit, raw silk, live-stock and marine products, and timber, the average annual imports of which amount, in value, to some 800 million dollars. The object is to reduce these imports by substituting native products. The public is urged not only to buy native goods but to invest in native industries.

207. Incorporated in this plan is the State iron and steel works for the construction of which a preliminary agreement was signed in January 1932 between the Ministry of Industries and the German firm of Gutehoffnungshütte of Oberhausen. In August this year the Ministry stated that preliminary investigations had been completed and detailed plans drawn up, but so far as is known no final contract has yet been signed (see annual report for 1933, paragraph 253).

208. In February the Central Political Council approved the reallotment of £250,000, originally allotted from the British Boxer Indemnity Fund for an ammonium sulphate factory (see annual report for 1933, paragraph 253), plus a further sum of £80,000 from the same source, for the establishment of a paper mill and hydro-electric plant. Preliminary investigations are being carried out in conjunction with the German firm of Siemens (China) (Limited) and the Chekiang Provincial Government. Work on the construction of a national alcohol factory at Pootung, near Shanghai, was started in February and is expected to be completed early in 1935. Investigations are also being conducted by the Ministry with a view to the establishment of a State woollen mill, and experiments are in progress with modern kilns for porcelain manufacture. The ammonium sulphate factory for the construction of which the Ministry was negotiating with British and German interests (see annual report for 1933, paragraph 253) is now to be undertaken as a private Chinese enterprise.

209. The Ministry has taken steps to reorganise the tea industry, and the enforcement of some form of State control is under consideration.

- 210. The Ministry appears to have confined its operations to those more purely industrial sections of the Four-Year Plan which do not duplicate the activities of the National Economic Council under the technical advisers of the League. The council has made considerable progress with work on the fundamental problems of rural reconstruction, land reform, water conservancy and road building, which, if persisted in on an adequate scale, should eventually effect a radical improvement in the economic condition of the country. Efforts have been made, in particular, to reform the silk industries and to establish the cotton industry in the north-western provinces on a wider and sounder basis.
- 211. The nine Sung Sing cotton mills have been in serious financial difficulties and are carrying on a hand-to-mouth existence. They are mortgaged to the banks for over 20 million dollars, and are believed to have unsecured debts to the extent of about 15 million dollars. Rumours have been current that these mills would be taken over by the Government, or that they and other native mills would be subsidised by a return of import duty on raw cotton or of consolidated tax, but later information is to the effect that such subsidies have not been, and are not likely to be, paid, though the Sung Sing mills were allowed to postpone payment of the consolidated tax. The export trade of the Japanese and British, as well as the native, mills in China has been adversely affected by the large increase in the import duties on raw cotton, which have been maintained in spite of protests from the foreign and Chinese millowners. Proposals to increase the consolidated tax on cotton yarn are now under consideration. Apart from an increase in revenue, the higher duties have resulted in more extensive use of Chinese cotton, of which the crop has been good this year.
- 212. Much attention has been paid to the extension of rural banking facilities and co-operative societies. Apart from the activities of the Ministry of Industries and those of the National Economic Council, the Chinese Government has made great progress in extending and unifying telephonic and telegraphic communications. Efforts to increase native interests in mining, to create a national mercantile marine, to extend the railways, to obtain a share in or control of business in foreign exchanges and to promote aviation are reported in other sections.
- 213. In addition to these measures of national reconstruction, which have, in fact, been mainly applied in the Yangtze Valley and the north-west, a number of the provinces have been promoting separate and often conflicting schemes for reconstruction, in particular, Shansi and Kwangtung. In Shansi the Five-Year Plan, started some two years ago, appears to be making steady progress with German and Japanese collaboration. In Kwangtung extensive industrial developments are in progress. Messrs. Skoda Works received early in the year a 2 million dollars contract for the erection of the third of a series of sugar refineries (see section on Customs), and Siemens China Company signed a 2½ million dollars contract for the supply of a new electric power station at Canton, with an option to construct a hydro-electric plant outside Canton at a cost of 20 million dollars. In addition to the iron and steel works (referred to below), an alcohol factory is in process of erection, and woollen mills and other enterprises are being promoted.
- 214. There has been a tendency, through monopolistic measures of control and other means, to impose undue restrictions on legitimate foreign trade. Amongst such measures have been various provincial regulations governing the sale of artificial fertilisers, which, apart from additional local taxation in Kwangtung and Fukien, have been obnoxious because they have often included attempts to fix selling prices and have in some cases been accompanied by unfair propaganda in favour of natural native fertilisers. Measures in force in Fukien and Kiangsi to prevent kerosene oil from reaching the "Communist" areas, though on the whole equitably applied, have given rise to similar objections. In the case of sulphuric acid, which is classed on the import list as a munition of war and is subject to special restrictions, a definite sales monopoly has been set up in Hupeh, and it is intended that similar monopolies shall be instituted in other provinces. The Legation has protested on general and on treaty grounds against this monopoly. It is, however, controlled by the Salt Administration without any apparent present intention to discriminate in favour of the native product as against either imported acid or acid manufactured in China by foreign firms.

- 215. Definite discrimination in favour of native manufactures has, however, been apparent in new legislation, as, for example, the new Law for the Encouragement of Industrial Enterprises, under which certain "rewards," consisting of exemption from taxation, rights of monopoly manufacture, and so on, are granted only to concerns which are 100 per cent. Chinese. This Legation has pointed out that to discriminate in this way against Sino-foreign industries established in China is not only unfair to such industries already established, but is also contrary to the declared intention of the Chinese Government to invite foreign capital investments in China as a means to nurture her nascent industries and to reduce her adverse trade balance. A similar intention to discriminate against foreign undertakings is to be observed in the arrangements recently made for through rail and steamship transport by the Ministry of Railways and certain Chinese shipping companies (see section on Shipping).
- 216. An even more pronounced protectionist policy has been manifested by some of the provinces, as, for instance, Kwangtung and Shansi, where the Provincial Governments have issued, but not yet enforced, protective regulations directed not only against foreign goods, but also against Chinese goods imported into the province from other parts of China.
- 217. The inclination to discriminate against foreign, or predominantly foreign, companies arises in part from a dislike of the extra-territorial privileges and diplomatic support which such companies enjoy, and the Chinese authorities have continued to bring pressure to bear on Sino-foreign enterprises to register under the Chinese company laws. The Kailan Mining Administration having been reorganised on a basis of equality as between the British and Chinese interests (see section on Mining), the Chinese Engineering and Mining Company, who constitute the British partner in the administration, has now been faced with the question as to whether a mining permit can be secured unless they register under the Chinese Company Law. The Mentoukow Mining Company is similarly being pressed to register, and the Tientsin Native Water Works Company (Limited) received in April a communication from the Hopei Provincial Bureau of Industries stating that a telegram had been received from the Ministry of Industry that the company be called upon to apply for registration according to the laws governing public utility companies. The question has not since been pressed by the Chinese authorities, but the company is considering the necessity for compliance. In the case of the (British) Kwong Sang Hong (Limited), of Hankow, who desired to register under article 43 of the Chinese Company Law, a purely formal certificate furnished by His Majesty's consulgeneral giving particulars of its registration under British law has proved sufficient for the purpose.
- 218. Illustrative of the strength of this growing spirit of nationalism are two applications from British limited liability companies for exemption from the requirement that in their Chinese names they state their British nationality and status. The first was made by the Imperial Chemical Industries (Limited), because the Chinese court in which they were appearing as plaintiffs refused to receive documents in Chinese describing the company as "limited" on the grounds that this description gave the erroneous impression that it was registered under the Chinese Company Law. The second, and more significant, application has been made informally by the British-American Tobacco Company (Limited), on behalf of the Yee Tsoong companies, newly formed with the express purpose of eliminating the words "British" and "American," which, in view of the "antiforeign feeling now rife," they find prejudicial to their business; they seek permission in the Chinese names of the new companies to omit the characters signifying "British company." It is improbable that the application could be granted under the law as it now stands, and it is proposed that the difficulty be met by an amendment of the Companies Ordinance. It is understood that the Imperial Chemical Industries (Limited), the China Printing and Finishing Company, and Butterfield and Swire are in favour of the proposal.
- 219. Repeated, but so far unavailing, representations have been made by the Legation regarding palpable imitations by 'Chinese manufacturers of the "Lux" trade-mark owned by Lever Brothers and the "Hazeline Snow" trade-mark of Burroughs, Wellcome and Co. The "Lux" mark had been duly

registered for soap; the Chinese imitation of the mark was registered for face cream. The "Hazeline Snow" mark had been registered for face cream; the Chinese imitation for soap. The Trade-Mark Bureau have consistently maintained that registration of a mark under one category only protects it against use by others on goods of the same category, and, moreover, have in the cases in question held that there has, in fact, been no deception of the public. Both British firms have repeatedly failed to obtain satisfaction from the Trade-Mark Bureau, and have been advised by their lawyers that neither a civil nor a criminal action in the courts would therefore serve any useful purpose. Messrs. Burroughs, Wellcome's appeal to the Ministry of Industries has been dismissed, and they are now appealing to the Executive Yuan. Messrs. Lever Brothers are appealing to the Ministry of Industries. The Minister of Industries has promised sympathetic consideration, but holds out little promise of success. He has stated, however, that the law on this point is in process of revision, though this will take a long time to accomplish.

- 220. British trade has been comparatively free from interference by boycotts, strikes, or anti-British agitation.
- 221. In Chekiang Province, in consequence, it is alleged, of the activities of the New Life Movement Promotion Society, violent agitation broke out at Haimen against the sale of British-American Tobacco Company cigarettes and of Imperial Chemical Industries (Limited) artificial fertilisers, and in August a similar campaign was started at Wenchow against sales of British-American Tobacco Company cigarettes. The origin and nature of the trouble are somewhat obscure, but so serious did it become that His Majesty's consul-general at Shanghai found it necessary to depute a vice-consul to remonstrate with the provincial authorities at Hangchow. The latter denied that there had been anything in the nature of an anti-British boycott. The trouble has now subsided.
- 222. A similar campaign, which was started last year, has been carried on throughout the country against the sale of the China Printing and Finishing Company's goods, on the grounds that the cloth used by the British firm is of Japanese origin. In spite of repeated representations, cloth seized in Chekiang at the end of 1933 has not yet been released. As is not uncommon in boycotts in China, seizures by the boycott associations have often been made from motives of self-interest and not from patriotism. In this connexion the company stated in January that, as the Japanese authorities give more efficient protection against boycotts of frankly Japanese goods than we are able to afford goods of a British company alleged to be of Japanese origin, Chinese dealers were prepared in some areas to buy cloth finished by the local Japanese works when they were frightened of purchasing cloth finished by the British company. An admission, made in confidence by the secretary-general of the Nanking Municipality in June, that all the members of the local Anti-Japanese Association were members of the Kuomintang and most of them also members of the Central or Municipal Government, is of interest. Though seizures of the China Printing and Finishing Company's goods have continued in various parts of the country throughout the year, the anti-Japanese boycott is apparently still active only in Yunnan. It is hoped that when the company's new factory at Shanghai is in full operation, and they are using their own cloth made in China, a stop may be put to these activities of the boycott associations.
- 223. In Shansi Province, the provincial cigarette monopoly, which last year threatened by methods of violence entirely to stop sales of British-American Tobacco Company and other cigarettes, has continued to operate, but owing to arrangements made through their Chinese associates in the province the British-American Tobacco Company have been enabled gradually to increase their sales over a wider area, and the position is no longer desperate.
- 224. On the 10th May the British Cigarette Company, on the grounds that long-continued insubordination on the part of the men had rendered further operation impossible, closed their No. 1 factory at Shanghai. On the 14th May agitators from No. 1 factory, supported by the labour unions and the local Kuomintang, who refused to listen to mediation by the mayor, entered the company's No. 2 factory and prevented work. On the 4th June workers were forcibly prevented by union pickets from entering No. 2 factory, and a fracas

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ensued, in which five of the company's foreign employees were injured. The mayor's proposals for adjustment of the dispute were unacceptable to the company, and both factories, which were continuously surrounded by a threatening crowd of pickets, remained closed. The mayor stated that the trouble was as much a political agitation engineered by the Tang Pu against the local authorities as a strike against the company. Intervention, at the request of His Majesty's Minister, by the generalissimo was apparently without effect. Towards the end of June various ad hoc organisations allied with the labour union endeavoured to start a boycott of the company's goods. The company maintained a firm attitude and a satisfactory settlement was eventually reached and work resumed in both factories on the 23rd July. Some 6,000 men had been meanwhile thrown out of work.

- 225. Serious trouble was experienced in Shantung during the first three months of the year by the British-American Tobacco Company, as the result of an order issued by the chairman of the provincial Government to his subordinates to encourage the sale of native cigarettes and discourage the consumption of foreign-made cigarettes. Violent measures were in some districts employed and the company's business suffered severely. Official representations by His Majesty's consul-general were without effect, but by March the movement had died down. It appears to have been a manifestation of provincial industrial chauvinism similar to those which have been experienced in Shansi and Kwangtung, the immediate motive for action being surplus stocks of tobacco leaf left on the hands of the farmers who expected to sell them to the British-American Tobacco Company. Full particulars have not been received by the Legation, but as the provincial officials are presumably personally interested in the provincial "native" factories it is not unlikely that further trouble will occur.
- 226. At Tangshan in Fukien the British-American Tobacco Company sales were seriously affected for many weeks in the spring owing to the activities of the local New Life Movement Promotion Society. Strikes and boycotts against British mining and shipping interests are referred to under the shipping and mining sections of this report. The handicaps from which British and other foreign trade has suffered owing to the increase and frequent changes in tariffs and taxation are referred to in the customs and the taxation sections of this report.
- 227. The following are some of the principal enterprises with which British firms have been concerned during the year. Vague schemes for the industrial development of Kwangsi and Kweichow on a large scale by a Sino-British financial corporation have been pressed by a member of the Kweichow Economic Commission, but appear unlikely to materialise. It is hinted that if British support is not forthcoming, the provincial authorities will turn to others for assistance. A preliminary agreement made in 1933 between the Yangtze Corporation who are affiliated to the Peking Syndicate and the Young Brothers Banking Corporation, for the industrial development of Szechuan, was confirmed in London this year, but it is now understood that, after consideration by the Ministries for Foreign Affairs, Finance and Industries, the bank has been instructed to cancel the agreement.
- 228. On the 1st July Messrs. Arnhold and Co. signed a contract with the Canton Government for the erection of a factory to produce ammonium sulphate, nitric acid and allied chemicals. The cost of the plant will be £114,000: an initial payment of 10 per cent. was paid with the order. Though the factory is probably required mainly for the production of munitions, no complaint has been made by the Nanking authorities.
- 229. A contract for the construction of a projected Kwangtung iron and steel works is being sought by British interests. The negotiations, however, involve a loan on security which, for political and other reasons, is of doubtful value. Moreover, as the specifications call for works readily convertible into an arsenal, there seemed reason to suppose that such a loan might be objected to by the Central Government, which has notified the foreign representatives that it regards unauthorised provincial loans as invalid. The agreement for the Shanghai–Hangchow–Ningpo Railway completion loan (see section on railways) provides that in the case of materials purchased from abroad preference will be

given to the tenders of parties recommended by the syndicate, and it is understood that the China Development Finance Corporation has agreed to exchange letters with the British and Chinese Corporation stating that this shall mean preference for British materials. Messrs. Dorman Long and Associates were informed by the commission in charge of the work that they were the "first selection" and Messrs. Siemens the "second selection" amongst those tendering for the superstructure of the new Chien Tang River Bridge, an essential feature in the completion of the Shanghai–Hangchow–Ningpo Railway. There ensued long and confused negotiations, in the nature of auctioning the contract to the two "selections," in which the Chekiang provincial authorities and the Ministry of Railways were both involved, though the status in the matter of neither was clearly defined, and in the course of which both parties substantially reduced their original tenders. At the moment of writing the contract has not yet been signed, but it is understood that it will be awarded to Messrs. Dorman Long and Associates.

230. No comprehensive contract has been made for the construction of the Canton-Hankow Railway (see paragraph 227 of annual report for 1933). Equipment obtained with the funds at the disposal of the Purchasing Commission of the Board of Trustees of the Boxer Indemnity Fund in London must, however, of course, be bought in the United Kingdom, and, with regard to the proceeds of the loan secured on the instalments payable to the board of trustees in London, a definite assurance was given in October 1933 by the Ministry of Railways that wooden sleepers required for the line would be bought from Canada or Australia. In connexion with tenders for Siamese sleepers this year, the Ministry of Railways has stated that these, if purchased, will be paid for out of funds other than the proceeds of the loan secured on indemnity payments. Large orders for Canadian and Australian sleepers have, in fact, been placed both for the Canton-Hankow and for other Chinese railways.

231. Substantial orders have been secured both in North and in South China for British woollen and other textile machinery.

VIII.—CUSTOMS AND TARIFFS.

232. For some time the Japanese have been pressing for the return to duty as chief secretary of Mr. Kishimoto, who had been granted extended leave of absence after the Mukden incident in 1931. The Japanese Minister, in conversation with the Inspector-General of Customs last January, reminded the latter of his written promise to reappoint Mr. Kishimoto as chief secretary, if the Chinese Government were willing and conditions of the service permitted. These two conditions could not be fulfilled at that time, and Sir Frederick Maze had begged the Japanese Minister not to press him too hard. Accordingly, when Sir Frederick Maze left China on leave at the end of March, Mr. Lawford, a British subject, was appointed officiating inspector-general ad interim during his absence. Mr. Ting, who was at that time Chinese secretary, was appointed chief secretary in the place of Mr. Lawford, who had been acting in that capacity since Mr. Kishimoto's departure.

233. At the beginning of December it was announced in the press that Mr. Kishimoto had been appointed Commissioner of Customs in Tientsin. During His Majesty's Minister's visit to Shanghai the Japanese consul-general at Nanking drew the attention of Sir Alexander Cadogan to this report. Mr. Suma stated that he had recently received assurances both from the Minister for Foreign Affairs and the Minister of Finance to the effect that there was no objection to Mr. Kishimoto resuming his duty as chief secretary; the Japanese Ambassador in London had, on instructions from his Government, expressed the hope to Sir Frederick Maze that Mr. Kishimoto would return shortly. Mr. Matsudaira had reported that Sir F. Maze had concurred and had promised to telegraph accordingly to Mr. Lawford.

234. Mr. Lawford subsequently confirmed to His Majesty's Minister the report of Mr. Kishimoto's appointment to Tientsin, which he said had been made as a result of the refusal of the Minister of Finance to have him back as chief secretary. Mr. Ting had recently been confirmed as officiating chief

secretary, although he had not vet been officially gazetted as chief secretary. Mr. Lawford added that he had received a telegram from Mr. Kishimoto saying that he was applying for an extension of leave, which he intended to grant. His Majesty's Minister expressed the hope that matters should be left as they were until Sir Frederick Maze's return in January, and that nothing should be done to make Mr. Ting's appointment more definite. Mr. Lawford concurred

On the 1st February, on the orders of the Chinese Government, the customs introduced new standard weights and measures. At the request of British importers, representations had been made by this Legation with a view to postponement of the new system until July. These representations, however, proved unavailing, whilst the new regulations have in practice given rise to no complaints or criticism.

236. The collection of the 5 per cent. revenue surtax (see paragraph 262 of annual report for 1933) was on the 23rd June extended till the 30th June, 1935.

The regulations for the marking of goods (see paragraph 264 of annual report for 1933) were on the 21st April indefinitely postponed.

Recommendations for an increase in tonnage dues (see paragraph 260 of annual report for 1933) were made in March by the commission appointed to discuss the question, but have not been published, and no effort has been made to put them into force.

A revised export tariff was published on the 21st June, the effect of which was to put on the free list a very large number of China's principal exports and substantially to reduce the duty on many others. With regard to goods which are exported in large quantities to the United Kingdom, the duties on eggs were reduced to a flat 5 per cent. ad valorem; woollen carpets and straw mats were put on the free list; the duties on bristles, hides and skins, wood-oil, tea, silk, camel's wool, silk piece-goods, wolfram and antimony and hats of buntal fibre remained unchanged. No explanation of the revision was given, but the reductions appear to have been confined to raw materials, and a few manufactured goods such as paper and carpets, thought capable of competing in foreign markets, and the motives were presumably to promote rural rehabilitation and to reduce the country's adverse balance of payments by an increase of exports.

It having transpired in the course of discussions initiated last year by the commercial counsellor with the Tariff Commission, with a view to reductions in certain items of the 1933 Import Tariff which adversely affected British trade, that the tariff was again to be revised this year, those discussions were continued (see paragraph 268 of annual report for 1933). These detailed discussions, which were principally connected with the duties on certain cotton and woollen piecegoods, woollen yarns, milk foods, machinery, and chemicals, resulted in certain recommendations for reduced rates, on items not competitive with native goods, which the representative of the Tariff Commission agreed he would submit to the Ministry of Finance. By April, however, it had become apparent that the National Tariff Commission was without effective influence, that the Ministry of Finance acted merely as a collector of revenue, that a body of politicians in control of the Legislative Yuan, inexpert in such matters, actually decided all policy, and that strong pressure was being exercised by the Japanese.

241. Towards the end of May His Majesty's Minister discussed the question with the Minister for Finance. The latter stated that he proposed shortly to submit the recommendations of the Tariff Commission, which included reductions on milk foods and certain types of cotton piece-goods made in United Kingdom but not in China, to the Legislative and Executive Yuans. He added that revision of the woollen sections was under consideration and that he was not in favour of increasing the rates on machinery.

242. The changes introduced by the new import tariff put into force on the 3rd July may be summarised as follows:-

(1) Reductions in the duty on certain classes of cotton piece-goods, principally, however, in the printed sections which chiefly interest the Japanese;

(2) Large increase in the duty on raw cotton, presumably as a protective

measure for the native product;

(3) A slight reduction on woollen piece-goods, but a considerable increase on lower value woollen yarn and thread, imports of which from the United Kingdom amounted to 8,500,000 dollars in 1933;

(4) No change in the duties on silk and artificial silk;

- (5) Increases of from 10 per cent. to 50 per cent. on metals, and general increases in the duties on electrical materials (other than bulbs);
- (6) Increases of from 33½ per cent. to 50 per cent. on machinery, one of the items the duties on which we were particularly anxious to see not raised;

(7) Duties on vehicles and vessels unchanged;

(8) General decreases in duties on fishery and sea products, mainly beneficial to the Japanese, but an increase on salt fish, the duties on which for the sake of the Canadian trade we were anxious to see lowered;

(9) General increases on animal products, groceries, cereals and fruits, &c. (affecting imports from Australia and Canada);

(10) General increases on chemicals and pharmaceuticles; as also on-

(11) Dyes and paints;

(12) General increases on timber, wood, &c., which adversely affect, in particular, imports of softwood from Canada and of rattans from the Federated Malay States;

(13) Slight reductions on paper proving very beneficial to imports of cheap Japanese newsprint but of no assistance to Canadian paper;

(14) Duties on sugar, cigarettes, and tobacco leaf unchanged;
(15) Duties on wines and spirits practically unchanged;
(16) Duties on oils, soaps, candles, &c., mostly unchanged;

(17) General small increases on most other goods.

- 243. The main object of the revision appears to have been a desire to obtain large revenue. This has not been the result, though it is not clear to what extent, if any, the diminution in revenues is to be attributed to restriction on imports due to the higher duties. No attempt was made to lower the very high duties on goods such as artificial silk, sugar and spirits, which have proved so strong an incentive to smuggling. There is little indication that the revision was designed to protect native industries, which have opposed both the increases on raw cotton, metals, chemicals and dyes, and the decreases in the duties on imports of cotton piece-goods and paper.
- 244. Some attempt has been made to meet our wishes for a reduction on certain classes of piece-goods and appreciation of substantial reduction on milk foods has been expressed by British importers. The decreases in the duties on cotton piece-goods are proportionately more considerable and affect a much larger volume of imports in those classes in which the Japanese are most interested, than those imported from the United Kingdom, while the increase in the duties on woollen yarn, machinery, metals, chemicals, and timber, adversely affects imports from United Kingdom sources more seriously than those from Japan. Decreases on fishery products and paper are actually only beneficial to Japan. The new tariff has been denounced, particularly in the South-West Provinces, as having been dictated by Japan, though in fact there appears to have been no intentional discrimination, the concessions to the Japanese being in the nature of levelling out those increases in the 1933 tariff, the incidence of which had fallen mainly on imports from Japan.
- 245. The higher import duties have led to a great increase in the contraband trade which is widely extended, well organised, and on a large scale. It affects all goods and all districts but the principal centres of trouble have been the following: Shanhaikuan and the passes on the Great Wall between China and Manchukuo, in connexion with the passage of Japanese goods and opium from Jehol. From Dairen sugar, artificial silk yarn and other commodities have been smuggled in large quantities into Tientsin and Shantung, whilst Japanese and other goods have similarly been introduced into Fukien from Formosa. In Kuangtung the position is extremely serious from our point of view, since the contraband goods mostly reach Kuangtung from Hong Kong. The semi-independent status of the province affords an incentive to cheat the Central Government of the customs revenues, and there is no doubt that the provincial authorities and local officials are directly concerned. Dr. T. V. Soong, in fact,

definitely stated to His Majesty's Minister last year that the head of the smuggling organisation was a brother of Chen Chi-tang, the *de facto* ruler of the province. Raw sugar for the provincial refinery has been regularly imported in large quantities without tax in ships of the Canton navy, one of which was recently fired upon and sunk by a customs preventive launch. The smuggling of opium, spirits and unmanifested cargo, which is principally composed of sugar, by ships of the Canton navy has become so prevalent that the Governor of Hong Kong has refused them the courtesy of the port. Persistent but unfounded rumours that negotiations for the transfer of the Canton customs-house to Hong Kong are to be resumed, have apparently been spread by the provincial authorities with the express purpose of rousing local opposition to make it clear that no such measures would be tolerated (see paragraph 261 of annual report for 1933).

- 246. With regard to Shantung, into which goods are smuggled by junks and small motor-boats from Dairen, eventually reaching Shanghai and other markets by the Tientsin–Pukow Railway, the Japanese naval authorities have hinted very strongly that they will not tolerate interference by Chinese preventive cutters outside the 3-mile limit. Customs preventive officers were instructed to avoid an incident, and in May new regulations were issued to deal with the junk traffic. In connexion with the contraband trade in Shantung grounds are not wanting for the suspicion that the piracy of the steamship Shuntien was organised by the Japanese secret service in Tientsin as a protest against the activities of the customs preventive cruisers off the mouth of the Yellow River.
- 247. Detailed regulations governing the duty-free import of supplies (other than munitions of war) for the use of foreign naval and military forces in China were communicated by the Ministry for Foreign Affairs to the Legations concerned in April, and it was later stated that these regulations would come into force on the 1st January, 1935. Whilst such supplies, except as regards the forces stationed in North China under the protocol of 1901, are not entitled as of right to duty-free import, this Legation in concert with the other Legations replied that the regulations after consideration by the naval and military authorities concerned had been found to be impracticable and could not be accepted. In reply to a further communication from the Ministry for Foreign Affairs in November pointing out that serious losses had been incurred in customs revenue by abuse of the privileges in question by certain individual members (nationality not stated) of foreign armed forces in China, this Legation put forward to the Ministry a simplified scheme devised by the British naval and military authorities and acceptable to the customs which was designed to obviate abuses of the nature referred to.
- 248. The imposition on the 15th October of a high export duty on silver (see section on Finance) has led to serious smuggling, the extent of which it is difficult to gauge. The Chinese Government has asked that measures be taken to prevent the export of silver from Hong Kong, alleging that an organised industry in refining smuggled dollars there for export has been established in the colony.
- 249. Executive action by the local officials at Tengyueh in connexion with the smuggling of gold into Burma led early in the year to temporary cessation of trade across the frontier.
- 250. A Customs Preventive Law was promulgated and enforced on the 19th June, and revised Regulations governing the Entry and Clearance of Vessels and the Presentation of Manifests and other Ships' Papers were issued by the Customs, with the approval of the Chinese Government in September. The object of these measures is to facilitate control of contraband trade and to increase the penalties for smuggling. On the whole the provisions are not unreasonable, though right of search within a 12-mile limit is claimed and has been exercised. The views of the British shipping companies, who have objected principally to the provision for the confiscation of a ship in circumstances not contemplated by the penal clauses of the treaties and to the fact that the Customs are given no discretion to waive fines, have been brought unofficially to the notice of the Chinese authorities with an informal general reservation of our treaty position.
- 251. Customs-houses have been opened at the passes along the Great Wall to prevent contraband entering through Manchukuo and Shanhaikuan.

252. The preventive service now has twenty-six seagoing craft (including sixteen new ones), in addition to a large number of launches and converted motor-boats captured from smugglers.

253. Schemes for the provision of a customs wireless service, and a preventive air force, are under consideration, but held up for lack of funds. A proposal for the air service was made last year by the Far East Aviation Company, and has recently been under discussion in modified form by His Majesty's air attaché and the customs authorities.

IX.—Conservancy and Other Works secured on Customs Surtaxes.

(a) Haiho Conservancy.

254. In January the Chinese Government stated, in reply to enquiries by the foreign representatives concerned, that the uncompleted works of the Improvement Commission would be undertaken by a new Haiho Improvement Reorganisation Engineering Board composed of conservancy experts selected by the Ministry of the Interior in conjunction with the Hopei Provincial Government.

255. A sum of about 2 million dollars was required for the work. The defunct Improvement Commission had originally proposed and the Diplomatic Body had agreed that the funds should be obtained from an addition to existing dues, and an increased surtax amounting to 8 per cent. on customs duties had been imposed for this purpose. As the result of pressure from the North China River Commission and from the Hopei Provincial Reconstruction Bureau, the members of which made the requirements of the palliative scheme an occasion for peculation, the Executive Yuan in February sanctioned the continuation of the surtax for a period of five years.

256. This action brought to light a divergence of views among the foreign representatives with regard to this, and other, local ad hoc local levies in the form of surtaxes on customs duties. The Japanese Minister informed the senior Minister that he considered "it desirable that the Diplomatic Body notify the Chinese Government that the imposition of the surtax in the future should be made conditional on the approval of the Diplomatic Body." This letter was not commented on and remained unanswered, but this Legation held that the proposal was inadmissible in view of the Foreign Office opinion expressed in 1930 that "the effect of the Tariff Autonomy Treaties of 1928 would appear to be to restore to the Chinese Government full liberty of action as regards both the taxation to be levied for conservancy purposes and the particular scheme or schemes to which the proceeds of such taxation are to be applied."

257. A decision on this aspect of the Haiho conservancy problem was, however, obviated by the acceptance of an offer made in March to the consular body in Tientsin by the Ministry of the Interior to carry on the work under the supervision of two engineers and two treasurers, one Chinese and the other a foreigner in each case, provided the interested foreign representatives made no objection to the continuance of the tax. Difficulties arose regarding the powers of the foreign engineer and treasurer, and, owing to the failure of the provincial authorities to prevent interference with the arrangements made to stop silt-laden freshets from entering the harbour, the river once more became unnavigable for ships drawing more than 9 feet. The secretary of the Haiho Conservancy Commission enlisted the support of the Officiating Inspector-General of Customs and of the National Economic Council. At a meeting of the latter on the 26th September it was decided to leave the release of funds for the completion of the palliative scheme in the hands of the Minister of Finance.

(b) International Bridge Surtax at Tientsin.

258. This surtax of 2 per cent. on customs duties was originally imposed with the approval of the Diplomatic Body in 1923 to provide funds for the construction of the International Bridge. That bridge having been duly completed, however, the surtax was in 1927 continued, with the consent of the

Diplomatic Body, for the purpose of constructing another bridge, the Hsi Ho Bridge, until such time as the requisite sum, estimated at 250,000 taels without the approaches, had been collected.

259. On the 1st September, 1934, a sum of 507,490 dollars had been collected for this purpose, which appeared to be sufficient. The Tientsin General Chamber of Commerce, however, had reason to suppose that the Chinese authorities proposed to continue the collection of the tax, with a view to financing other schemes which they considered should not be proceeded with until certain abuses in municipal administration had been eradicated. The question was taken up by the consular body, which put forward to the Diplomatic Body a proposal, in which the British consul-general felt constrained to concur, that the Ministry of Finance be moved to instruct the Commissioner of Customs to cease the levy of the surtax on the grounds that adequate funds had already been collected to finance the construction of the Hsi Ho Bridge, for which purpose the continuance of the surtax had been sanctioned in 1927. As in the case of the surtax for the Hai Ho Conservancy, there was diversity of opinion amongst the foreign representatives. This Legation held that, in view of the opinion expressed by the Foreign Office, that the effect of the tariff autonomy treaties was to restore to China full liberty of action in regard to taxation for conservancy purposes, no official representations could be made, and also that the moment was inopportune for raising the question informally, since the construction of the Hsi Ho Bridge has been approved by all concerned, and there was, in fact, no evidence that the Chinese proposed to prolong the surtax for other purposes. The American and Italian Legations were in favour of individual informal representations, with a view to ascertaining the cost of construction, and cessation of the surtax so soon as the requisite sum had been collected. The Japanese, French and Belgian Ministers were of the opinion that the surtax in question being a local levy its imposition was not covered by the treaties granting national tariff autonomy to China, and they proposed to make representations that the levy should cease.

(c) Chefoo Harbour.

260. In view of the attitude adopted by the Diplomatic Body when repayment of the 1918 loan had first been demanded by the Customs in 1932, and in accordance with the stand taken by this Legation towards these conservancy questions since the tariff autonomy treaties, it was felt that no formal action could be taken in connexion with the renewed demand for repayment made by the Ministry of Finance in November last. The commercial counsellor, however, informally represented to the Inspector-General of Customs that, as the commission were to an extent still to be determined committed to contracts for harbour improvements, the demand seemed inopportune. At the same time, the foreign representatives requested the Netherlands Minister, then at Nanking, to make informal representations to the Minister of Finance on behalf of the Diplomatic Body. He went so far as to state that the heads of missions considered the demand for repayment to be contrary to the original 1913 agreement between the Chinese Government and the Diplomatic Body concerning the Chefoo surtaxes.

261. The refund was made early in December, and the attention of the Harbour Commission, now that it remains in possession of only 400,000 dollars and a net income of about 40,000 dollars, has been focussed on their position vis-à-vis the large contract of undetermined validity which the Netherlands Harbour Works Company allege to have been made. In June the company demanded immediate action, either in the way of carrying out the contract, or of settling a claim for damages. The committee eventually decided to forward a revised provisional report and proposal, provided by the company, to the Ministry of Finance for transmission to experts of the Ministry of Communications. An expert from the Ministry of Railways did visit the port in August, but appears to have been non-committal, and there, so far as is known, the matter rests, the activities of the commission being meanwhile confined to necessary dredging operations.

(d) Other Works, &c.

262. Work on the conservancy of the Whangpoo, and on the Min River, has progressed satisfactorily, and no questions have arisen in connexion with these surtaxes. Half-hearted proposals by the French and American Legations, that protests be made against the dissolution of the Liao River Conservancy Board (see paragraph 276 of annual report for 1933), were eventually dropped.

263. This Legation has not so far been directly concerned with the formation by the Chinese Government of a National Conservancy Board, under the National Economic Council, nor have the functions of the council so far interfered with conservancy operations in which this Legation is concerned, as being secured on surtaxes concurred in by the Diplomatic Body.

X.—BOXER INDEMNITY.

- 264. Early in the year the Chinese Government, after first ascertaining that it would be agreeable to His Majesty's Government in the United Kingdom, reappointed for a further period of three years the four British members of the London Purchasing Commission (Sir A. Balfour, Sir B. Blackett, Sir R. L. Wedgwood and Mr. G. A. McEwan), whose terms of office expired in April. In the summer Mr. E. R. Hughes resigned from the board of trustees in China, and Mr. J. B. Taylor of the Nankai University, Tientsin, was appointed to the board, the foreign members of which now also include Mr. N. S. Brown, Mr. R. Calder Marshall and Mr. W. S. King.
- 265. In June it was announced that the Educational Sub-Committee of the board of trustees in China had decided to distribute the sum of 1,200,000 dollars out of the interest funds which had accumulated during the past three years to some 1,300,000 dollars. Of the grants made, 180,000 dollars was allotted to scholarships for Chinese students in the United Kingdom, nine students having been sent in 1933 and thirty-one more being due to follow this year. Subsidies to institutions included 1,150,000 dollars to the National Central Museum and the National Central Library respectively, of which 150,000 dollars only was to be paid in advance during the present year; in addition, 120,000 dollars to be paid in three equal annual instalments were allotted to the Sun Yat-sen University at Canton.
- 266. By the 14th June the Chinese Government paid off the whole of the balance owing in respect of the two months' arrears of payments which occurred last year (see paragraph 279 of the annual report for 1933).
- 267. The flotation on the 1st August of a loan in pursuance of the agreement signed by the board of trustees in 1933 for the completion of the Canton-Hankow Railway is reported in the section on Railways. This loan is secured on two-thirds of the annual instalments payable to the board in China, the remaining one-third being mainly used to finance various conservancy schemes, on which work is now actively in progress.
- 268. The board of trustees have this year voted a sum of 20,000 dollars for premises for the Sino-British Cultural Association in addition to a grant of 60,000 dollars for three years to enable the association to invite British lecturers to China. Steps have accordingly been taken to establish a club-house and to secure six lecturers on scientific and other subjects, two of whom have already arrived in China. The membership of the association now stands at some 120 members, of whom about half are British subjects.
- 269. On the 26th January an agreement was signed between the Ministry of Finance and a syndicate composed of a number of Chinese bankers for a loan of 44 million dollars secured on the remitted instalments of the Italian indemnity. The loan it is understood represents about two-thirds of the total remitted Italian indemnity, the remaining one-third of which is to be used for the purpose of aircraft and other war materals.

XI.—AVIATION.

Sales of Aircraft.

- 270. There continues to be considerable expansion of military aviation in China. The Aeronautical Affairs Commission has purchased 114 service aircraft (including thirty training type) of which 90 per cent. are of American manufacture. Although more aircraft have been imported from the United States than from any other country, contracts which have recently been made with Italian firms help to confirm that American interests are losing ground whilst the Italian position is being consolidated.
- 271. The number of sales of British aircraft which have been effected is comparatively few and confined chiefly to the Province of Kwangsi. Foreign competition is very severe, and in spite of efforts which have been made by the Far East Aviation Company to excite the interest of the Chinese in British products by means of demonstrations, &c., the results have been disappointing and future prospects are not encouraging. No sales have been effected either by Messrs. Arnhold and Co. (representing Messrs. de Havilland Aircraft Company), who closed down their Aviation Department in June, by Messrs. Jardine Engineering Corporation (representing Messrs. Vickers (Aviation) (Limited) and Messrs. Bristol Aeroplane Company (Limited)) or by Messrs. Reiss, Massey and Co. (representing the Hawker Engineering Company and Messrs. Rolls Royce (Limited)).
- 272. United Kingdom representatives complain of the disadvantage at which they are placed vis-à-vis their Italian competitors, and submit that they are unable to accept credit terms extending over periods varying from two to five years unless they receive financial backing from His Majesty's Government in the United Kingdom. They contend that the success which the Italian manufacturers have achieved in obtaining contracts is due to what virtually amounts to Sino-Italian inter-Government trading, with the Italian Government guaranteeing the credit terms offered by the Chinese National Government. American interests, which have been in a predominant position until recently, are apprehensive of the influence and success which their Italian competitors now enjoy.
- 273. Proposals for an auxiliary air arm for the Chinese Maritime Customs Preventive Service (see paragraph 288 of last year's report) were discussed by the air attaché and the Inspector-General of Customs. The scheme is still under consideration.

The Far East Flying Training School, Hong Kong.

274. Ten Chinese students are being trained as pilots on Avro Cadets and thirty-seven Chinese are taking the ground engineering course.

Foreign Aviation Interests in China.

- 275. The Bureau of Aeronautics moved from Hangchow to Nanchang in April and has been reconstituted under the title of "The Aeronautical Affairs Commission" with Chiang Kai-shek as president. Colonel John Jouett, the head of the American Aviation Mission, who was previously air adviser to the National Government, has been succeeded by General Lordi, the head of the Italian Aviation Mission, who is now virtually chief of the Air Staff.
- 276. Propaganda flights by well-known American, Italian and French pilots have been made and undoubtedly assist in securing contracts. For instance, the French aviatrix, Mlle. Maryse Hilz, flew through China on her second Paris-Tokyo flight in March in a Breguet 27-3 Sesquiplane and a contract for ten aircraft of this type has been concluded with the National Government. Demonstration flights were also carried out by Commander Frank Hawks with a Condor (Curtiss-Wright Airplane Company, U.S.A.), by Lieutenant Dorsey of the United States Air Corps with a Boeing Fighter P-26a and by Mario de Bernardi with Caproni, Types 111 and 113 (Societa Italiana Caproni). In addition, a Junkers (Type Ju. 52/3m) was flown out from Berlin in August via India in eight days (sixty-nine flying hours), and demonstration flights have been given at Shanghai, Peking, Nanking and Nanchang to several hundred Chinese, including many prominent personalities.

277. The Curtiss-Wright aircraft factory (see paragraph 291 of last year's report) at Hangchow is now completed; it is anticipated that the capacity will be sixty airframes per annum, but the engines will be imported from the United States of America. A site has been selected at Kiukwan (Kwangtung) for another Curtiss-Wright aircraft factory, and equipment and machine tools (estimated value 750,000 gold dollars) have arrived at Hong Kong. Negotiations for the erection of a Sino-German aircraft factory in co-operation with Junkers are, however, temporarily suspended, the Italian Aviation Mission being also interested in a similar proposition.

Foreign Aviation Missions.

278. The Central Aviation School, Hangchow, has been greatly developed, but, owing to Italian influence, it is unlikely that the three-year contract with the American Aviation Mission (which expires in May 1935) will be renewed. Considerable progress has been made by the Italian Aviation Mission under General Lordi at Nanchang.

Air Routes.

China National Aviation Corporation.

279. This company's Yangtze air service (see paragraph 296 of annual report for 1933) has been extended from Chungking to Chengtu, four trips weekly being made in both directions. The Shanghai-Canton service, owing to a second serious accident, was suspended in April, but was re-established in November. The fleet consists of two Douglas Dolphin amphibians, seven Loening amphibians and four Stinson Detroiter landplanes. The traffic for the first nine months of this year, as compared with the year 1933, is shown in the following table:—

Year.	Kilometres flown.	Passenger Kilometres flown.	Passengers carried.	Kilograms of Mail carried.
1933	1,024,963	1,451,384	3,050	49,246
	989,869	1,706,222	3,334	39,691

Eurasia Aviation Corporation.

280. Owing to political difficulties in Sinkiang, the Eurasia Aviation Corporation has been unable to extend the proposed Shanghai–Berlin air line beyond Lanchow, but a weekly branch service to Ninghsia and Paotowchen has been established. A twice-weekly service between Peking, Hankow and Canton was inaugurated in May. The fleet consists of seven Junkers landplanes.

Finances.

281. Although the China National Aviation Corporation and the Eurasia Aviation Corporation air services still continue to operate at a loss, considerable progress has been made in the development of air routes and the provision of modern aircraft and equipment. Funds for the development of aviation are allocated from the National State Lottery and the above-named operating companies are in receipt of a subvention from the National Postal Administration.

South-West Aviation Corporation.

282. A twice-weekly mail and passenger air service was inaugurated in October, between Canton and Lungchow, via Wuchow and Nanning. Air mails are also conveyed between Canton and Hoihow (Hainan). Whilst the China National Aviation Corporation is a Sino-American company and the Eurasia Aviation Corporation Sino-German, all members of the technical and administrative staffs of the South-West Aviation Corporation are of Chinese nationality. At present, the service is operated with three Stinson Reliant landplanes. It is interesting to note that Lungchow is only 25 miles from the French frontier of Tongking and 120 miles distant from Hanoi, having regard to a report that "Air France" intends to inaugurate an air service between Bangkok and Hanoi in

January 1935. This means that there will be only a short distance to be bridged between the existing air services in China and the projected route connecting Hanoi with the European air service operated by "Air France."

Survey Flight, Hong Kong-Bangkok (via Hanoi).

283. This flight was carried out in August by Captain Jones-Evans, D.F.C., of the Far East Aviation Company, Hong Kong. The report shows that there would be little difficulty from the flying aspect in establishing an air service on this route linking up Hong Kong with the London-Australia air route, provided multiengined air transports are used. The air attaché has had conversations with his Excellency the Governor of Hong Kong regarding this proposal. He also met the Under-Secretary of State for Air at Singapore in October when inter alia this question and the development of both military and civil aviation in China were discussed.

XII.—LEGISLATION.

- 284. During the year under review there was apparent a slackening in the flow of legislation promulgated by the Chinese Government and its subordinate organs.
- 285. The Legislative Yuan produced no fewer than three drafts of the Permanent Constitution of China, the final so-called New Draft being forwarded by the National Government to the Central Political Council in November. A new Criminal Code has been passed by the Yuan, but not yet promulgated, and revised Civil and Criminal Codes of Procedure are still under consideration. The two *interim* measures relating to procedure execution in civil cases, which were referred to in paragraph 304 of the 1933 report have now been officially placed on record by the Central Political Council. The Organic Law of the National Government underwent revision in consequence of the transfer of the Ministry of Judicial Administration (Ministry of Justice) from the Executive Yuan to the direct control of the Judicial Yuan.
- 286. As a result of the situation arising out of a dispute between the Executive and Control Yuans over the impeachment of Mr. Ku Mêng-yu, Minister of Railways, who was subsequently exonerated, the Central Political Council adopted a new ruling in November that the text of the impeachment brought by the Control Yuan, and the counter-reply of the impeached official would be simultaneously released; and that if the official impeached had been appointed by the Central Political Council, the judgment rendered against him should be submitted to the Central Political Council.
- 287. Various regulations were issued affecting shipping. The most important of these was the Customs Preventive Law of the 19th June, on which were based the revised regulations governing the entry and clearance of vessels and the presentation of manifests and other ships' papers (shortly called the "Revised Manifest Regulations") issued by the Maritime Customs in September. Certain of the penalties provided for, involving confiscation of goods and/or the vessel concerned, are extra-treaty, while their imposition is mandatory and not permissive as in the 1931 regulations which they replace. The whole question as regards the effect of the regulations on British shipping is now under consideration.
- 288. As regards the Regulations for the Control of Towed Vessels (paragraph 299 of 1933 annual report), an attempt was made by the Chinese authorities to enforce these on all foreign flag tows as from the 1st June, including those towed by vessels under river pass, but as the result of representations made by His Majesty's Minister instructions were issued by the Customs in the middle of June suspending their application (see section on Shipping). No attempt has been made to apply to British shipping companies Regulations Governing the Registration and Licensing of Wharf Boats (including Hulks and Pontoons) which were issued on the 28th April.
- 289. Among other minor shipping legislation not directly affecting British vessels may be cited the regulations of the 8th January for the Capture of Pirates and Protection of Vessels, Regulations Governing Wireless on Steamers, Revised

Regulations for the Measurement of Ships, promulgated the 28th October, 1933, and the Navigation Marks Ordinance (or Ordinance Governing Aids to Navigation) issued on the 15th May (but not yet enforced).

- 290. Various enactments have been issued by the Chinese Government on the subject of industry, including the Law for the Encouragement of Industrial Enterprises, promulgated the 20th April, together with the ancillary Industrial Enterprises Encouragement Scrutiny Committee Regulations of the 29th August, and the Industrial Enterprises Encouragement Scrutiny Standards of the same date, which took the place of the similar law of 1929 and ancillary regulations of 1930. Representations have been made to the Chinese Government regarding the discrimination involved in article 11 of the law, which debars from "encouragement" under the law any industrial enterprise in which foreign capital participates. Of lesser importance, but also indicative of the campaign to promote the industrial development of China by the Chinese, are the Rules Governing the Issue of National Goods Certificates by the Ministry of Industries dated the 6th June, and the Provisional Standards of Chinese National Goods of the 4th June.
- 291. A Revised Ordinance for the Supervision of Privately-operated Public Utility Enterprises was promulgated on the 2nd November, 1933, and Rules for the Control of Electrical Enterprises and a Revised Electrical Enterprises Ordinance on the 20th January and the 27th February respectively. One British company, the Tientsin (Native City) Waterworks Company (Limited), has been pressed by the Chinese authorities to register under the first-named ordinance, and is considering whether it can do so without prejudice to its status as a British corporation.
- 292. Reference to the enforcement of the Business Tax Law of the 13th June, 1931, on British subjects, and the Law of Publications of the 16th December, 1930, is made in the sections on Taxation and Propaganda respectively.
- 293. Various regulations have been issued on the subject of wireless telegraphy, covering the procedure for applications for huchaos for importing wireless materials, and the registration of the installation of wireless receiving sets
- 294. Educational and military matters have continued to form the subject of numerous legislative enactments. Especial attention may be drawn to rules promulgated jointly by the Inspectorate of Military Training and the Ministry of Education in June providing for a three weeks' course of special military training for all high school and university students during their summer vacation. Rules were about the same time issued making boy scout training compulsory in junior middle schools. The Military Secrets Protection Law, originally put into force for nine months as from the 1st April, 1933, has been extended until the end of the present year. In regard to education, the Ministry of Education on the 28th April issued orders that unregistered primary schools established by foreigners or foreign bodies prior to the promulgation on the 19th October, 1933, of the Revised By-laws Governing Private Schools might, subject to certain stipulations, be allowed to effect registration not later than the current scholastic year, i.e., that ending June last: no difficulties affecting British schools have, however, been brought to the notice of His Majesty's Legation.
- 295. The Census Law of the 12th December, 1931, came into force on the 1st July, and detailed enforcement rules were issued taking effect on the same date.
- 296. In a different category are the "Provisional Regulations Governing the Strict Prohibition of Narcotic Drugs," issued in May by General Chiang Kai-shek as chairman of the Military Affairs Commission. Offenders under these regulations are dealt with under martial law. The death penalty is laid down both for dealers in morphine, cocaine and heroin, and for addicts who do not break off the habit within a prescribed period, or having done so, later relapse.

297. Mention may also be made of the "New Life Movement" initiated by General Chiang Kai-shek at Nanchang in February, which has since been endorsed by the Central Party Headquarters and has been taken up with enthusiasm in all parts of the country. The movement aims at a greater simplification and rationalisation of life, manners and thought, by a return to the Confucian principles of Li ("Regulated Attitude or Propriety"), I ("Right Conduct or Righteousness"), Lien ("Honesty or Incorruptibility") and Chih ("Sense of Shame").

XIII.—PROPAGANDA.

- 298. The dissemination of official news and propaganda has, during 1934, been carried out by the same organs as described in the section on Propaganda in the annual report for 1933, and the Government seems to be able to keep a surprisingly effective control over the tone of the Chinese press. There have, however, been certain developments during the past year.
- 299. The Central News Agency started a daily news service in English at Nanking in September and at Shanghai in the beginning of October. Moreover, this agency has opened an additional wireless station at Nanchang. It appears that this was done at the instance of General Chiang Kai-shek who complained of the inaccuracy of military reports. The bureau at Nanchang, which has been granted a subsidy of 5,000 dollars a month, has been placed under the charge of the agency's editor-in-chief, Mr. Fan Yu-chen, and is apparently intended to be the press office of the generalissimo's headquarters.
- 300. The Kuomin News Agency, which is under the control of Waichiaopu, tried to come to an arrangement with the Central News Agency for a single united service in English, but without success. It appears that the Kuomin News Agency, despite its subsidy from the Waichiaopu, is not strong financially and may be in danger of disappearing.
- 301. A Central Censors' Bureau has been formed this year and placed under the National Defence Council. The chief censors are Yeh Chu-tsang representing the Central Party Headquarters and Tang Yu-jen, the Vice-Minister for Foreign Affairs, representing the Central Political Council. Under the Central Censors' Bureau are branch Censors' Bureaux at Nanking, Shanghai, Hankow, Peking and Tientsin.
- 302. The cinema is now being largely used by the Chinese Government as a medium for propaganda, and in Shanghai for instance, the majority of Chinese films being shown are typical Kuomintang propaganda, being undoubtedly meant for the labouring classes who are the greatest patrons of the Chinese cinema. The work of film censorship on behalf of the National Government has since March been carried out at Nanking by a Central Film Censorship Committee.
- 303. Radio continues to be used as a means of disseminating propaganda and foreign news is broadcast by the Transocean Kuomin Wireless Service in carefully prepared shape. In view of the increasing tendency of Chinese of all classes to purchase receiving sets this method of propaganda may develop into a strong and even dangerous weapon. All radio broadcasting stations are required to be licensed by the Bureau of Radio Administration established by the Ministry of Communications which grants the local Chinese authorities liberty to use the Chinese stations.
- 304. There has been no violent outburst of anti-British or anti-foreign propaganda in China during the course of this year. Even anti-Japanese comment has been comparatively mild. In its initial stages it looked as if the canvassing of the New Life Movement might lead to an access of anti-foreignism; but it appears that the Government authorities discouraged such exaggerations and that their controlling influence was generally effective. Soon after the despatch of the Burma expedition to the Wa States (see section on Burma), there was a minor agitation against this alleged "invasion" of Chinese territory, but with the progress of negotiations at Nanking, this agitation for the most part died down.

In fact when at the end of June the Chinese consul in Rangoon published an improper statement in the Rangoon papers accusing the expedition of crossing into territory claimed by China, the Central Government quickly responded to representations by His Majesty's Legation and recalled the consul. In Yunnan Province, however, the local papers have continued to foment an anti-British agitation and the attention of the Central Government has been drawn to the matter.

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305. His Majesty's consul-general at Canton reports that there has been a noticeable improvement in the standard of the three local official propaganda organs; namely the Min Kuo Jih Pao, the Kwong Chow Jih Pao and the Shih Min Jih Pao, which are controlled by the Provincial Kuomintang, the Municipal Kuomintang and the Municipal Government respectively. The Min Kuo Jih Pao in particular no longer restricts itself to criticism of Nanking, but also publishes constructive propaganda in regard to the achievements of the local Government and the progress of the Three-Year Plan, while there can also be found intelligent comments on international affairs. In addition the Propaganda Section of the South-West Executive Committee of the Kuomintang manages the Central Press News Agency which supplies a free news service to papers published in English in Canton, Hong Kong and elsewhere.

306. As much assistance as is possible continues to be given by His Majesty's Legation to Reuter's, with a view to meeting increased competition from the French News Agency, Havas, and the United Press and Associated Press of America. So far as is known to His Majesty's Legation, there have, however, been no new developments in 1934.

307. In accordance with instructions received from the Foreign Office, and after consultation with the United States Legation, a note was addressed to the Waichiaopu on the 14th February stating that His Majesty's Government in the United Kingdom had no objection to the voluntary pro forma registration of British newspapers and periodicals, required under the Chinese Law of Publications (see annual report for 1933, paragraph 317), but that it had no authority to compel British interests concerned to register. The reservation was, moreover, made that any such registration could not, in the view of His Majesty's Government, be held to involve acceptance of the penal provisions and administrative control contained in the Chinese law. On the same day the United States Legation addressed a similar note to the Waichiaopu. In October a communication was received from the Waichiaopu referring to our note of the 14th February, and stating that any Chinese or foreign newspapers and periodicals that failed to apply for registration with the Ministry of the Interior before the end of February 1935 would not thereafter be granted such facilities and reduced rates as are provided by the Chinese posts for newspapers. It is accordingly proposed to instruct His Majesty's consular officers to inform the British interests concerned of the contents of the Waichiaopu letter, and advise them to effect registration with the Ministry of the Interior and the approval by the Foreign Office of this proposal has been sought. In the meantime, in answer to enquiries made by the United States Legation, the Vice-Minister of the Interior has given assurances, which he emphasised were unofficial, that the registration by foreign newspapers would be purely on a pro forma basis, was required for statistical purposes, and did not imply any measure of administrative control. The United States Legation have accordingly communicated the Waichiaopu letter to United States consular officers in China for their information and, in informing the Waichiaopu of the action taken, have reiterated the statements and reservations made in their note of the 14th February.

XIV.—CLAIMS.

308. As regards the question of the action to be taken for the checking and settlement of the lists of accumulated claims in the Legation archives, instructions were received from the Foreign Office in November approving the second course of action set forth in paragraph 318 of the annual report for 1933, namely, that

the first step should be to seek to reach an agreement with the Chinese Government upon the principles which should govern the formulation of our claims. An early opportunity of carrying out these instructions will be taken.

- In the meantime representations are being made in respect of a number of claims and debts. On instructions from the Foreign Office the Chinese Government were requested to provide the 110,640 47 dollars outstanding in respect of the Nanking claims. In reply, the Waichiaopu refused to make this payment, and the Vice-Minister for Foreign Affairs, in conversation, expressed the earnest hope that His Majesty's Government in the United Kingdom would not press this matter, since the Waichiaopu had reported to the Chinese Government that all amounts due in respect of these claims had been fully paid. After further consideration, it was decided to inform the Chinese Government that, while His Majesty's Government must continue to press for the balance due to them, they would be prepared to receive it in sterling instead of in dollars. It was calculated that the sterling amount due should be computed at £6,218 5s. $1\frac{1}{4}d$., which, at present rates of exchange, would save the Chinese Government about 17,000 to 18,000 dollars on the 110,640·47 dollars previously demanded. In case the Chinese Government refused to accept this offer proposals are under consideration with a view to arranging that this question should be referred to arbitration. Representations have been partially or completely successful in the following cases:-
 - (a) A total sum of 43,800.63 dollars was paid for the six Pukow-Puchen individual claims in respect of losses incurred at the time of the Nanking incident in 1927. These claims had been assessed by the Sino-British Claims Commission in December 1929, after the assessment of the Nanking claims had been completed; but it had been decided not to press for payment of these claims until the Nanking claims, or at least the bulk of them, had been liquidated. It seems probable that the prompt payment by the Chinese of these Pukow-Puchen claims is not unconnected with the request that we should not press for the payment of 110,640.47 dollars still due for the Nanking claims.

(b) Mr. L. H. Gabb accepted a final additional payment of 3,000 dollars over and above the payment of 5,000 dollars paid to him in 1932 in settlement of his claim for injuries and losses inflicted by Chinese

troops at Chengteh in 1929.

(c) The total sum of 5,070 dollars was paid as a compromise settlement of the claims for damage done in January 1932 to two British ships, steamship Cape St. George and motor vessel Neptunian, as a result of an explosion of gunpowder belonging to the Shanghai arsenal while being towed down the Whangpoo.

- (d) In respect of an outstanding debt of 35,334.30 dollars, due from the Ministry of Finance to Messrs. E. G. Byrne and Co. for coal delivered in 1920-21, the Ministry, after repeated representations, provided a payment of 10,000 dollars in November, and a further 50,000 dollars at the end of the year in final settlement of the claim.
- 310. In addition, some British firms have been able by private negotiation to come to arrangements with the Chinese for the liquidation of their outstanding debts. On the 31st December, 1933, an agreement was signed between the Ministry of Communications and three British firms for the repayment of £16,605 0s. 9d. by monthly instalments of not less than £800 each. All instalments due up to the present have been promptly paid. Messrs. J. Whittall and Co. (Limited) also agreed to a compromise (the figure is not known) in final settlement of the debts owing to them by the Peking-Suiyuan Railway. In general, however, the prospect of British companies being able to negotiate more or less satisfactory settlements of the debts outstanding to them from the various Chinese railway administrations has not been enhanced during the course of this year owing to the extremely adverse settlements which certain Japanese and United States companies have apparently accepted (see section on Railways).
- 311. At the end of August His Majesty's consul-general at Shanghai received a communication from the Japanese consul-general giving a list of the

amounts which the Japanese Government were prepared to give as solatium to certain of the British claims for the losses suffered by them during the Sino-Japanese hostilities at Shanghai early in 1932, provided that they relinquished their claims. It was expressly stated that no liability was accepted by the Japanese Government. As a matter of fact, many of the British claims presented to the Japanese Government on the 10th January, 1933, found no place amongst the sums allotted, which amounted to 61,540·00 yen only, out of a sum of about 1 million dollars claimed. On the understanding, however, that better terms were not obtainable, most of the claimants expressed their willingness to accept the amounts offered by the Japanese Government, and authority was received from the Foreign Office to allow the settlement of these claims to go forward.

Minute Paper.

Register No.

P.Z

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SECRET.

POLITICAL DEPARTMENT.

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	Date.	Initials.	SUBJECT.
Under Secretary Secretary of State Committee Under Secretary Secretary of State		M	China Annual Report for 1933.

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FOR INFORMATION.

The prographs on Sinking (78-88) and on Tibet (89-98) are of Indian interest.

There is little else in the report of direct concum to Tudia, although The accounts given of developments in Manchenia (§§ 45-72), Sino-Japanese military operations (§§ 106-115), Waltons with the UK. (§§ 125-146) and propaganda (§§ 306-317) are of general interest.

Previous papers:

Wills Kws.

SEEN POLITICAL COMMITTEE.

3 AUG 1934

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Mr. Ingram to Sir John Simon.—(Received March 6.)

(No. 1.)

Peking, January 1, 1934.

Sir, I HAVE the honour to transmit herewith the annual report on China for the year 1933. I am indebted for the preparation of this report to the members of my staff, who have all contributed their respective sections and generally assisted in its compilation.

- 2. I trust that this report will not be considered unduly long, but owing to the many important events, in particular those regarding Sino-Japanese relations, which have occurred during the past year, it was felt that to have abbreviated it further would have deprived it of much of its value. The section on Manchuria has been somewhat amplified this year owing to the completely novel situation which has been created there and the wide interest which it has evoked.
- 3. I feel I cannot close this despatch without placing on record the regret expressed in all quarters at the departure of Sir Miles Lampson after seven years' service as His Majesty's Minister in China. Both in public and private glowing testimony has been paid during the last few months to his services in the cause of Sino-British friendship. The Chinese tributes to his achievements in this respect have, indeed, been universal and truly remarkable for their sincerity and warmth.

I have, &c. E. M. B. INGRAM.

Enclosure.

Annual Report on China for 1933.

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I.—INTERNAL POLITICAL SITUATION.

(1) General.

THE year 1933 has been another eventful one in China, and, while the framework of the National Government remains unaltered, the general background of the political scene has undergone momentous changes. As in 1932, the internal situation has been so closely interwoven with the relations between China and Japan as to make it impossible to review the one without touching at some length on the other.

The position at the beginning of 1933 as regards the composition of the National Government was as follows: Lin Sen still occupied the figure-head post of President (Chairman of the Government), while Chiang Kai-shek retained his position as head of the Military Commission, a post which carried with it that of Commander-in-chief of the National Forces, thus enabling General Chiang to maintain his military supporters in key positions in the country and thereby keep his controlling voice in national affairs. Nominally the Government was still a coalition, and embraced the recalcitrant Cantonese elements with whom Nanking had come to terms after the crisis with Japan, including Wang Ching-wei as head of the Executive Yuan, a position corresponding to that of Premier in other countries. Actually, however, Wang Ching-wei had retired abroad following his differences with the young marshal (Chang Hsueh-liang), who remained in control in North China; so that the foundations of the Government rested again in practice on the shoulders of Chiang Kai-shek, assisted by his brother-in-law, T. V. Soong (Sung Tzu-wen), as Minister of Finance and acting head of the Executive Yuan, and Lo Wen-kan as Minister for Foreign Affairs. Hu Han-min, the third member, with Chiang Kai-shek and Wang Ching-wei, of the triumvirate of the Standing Committee of the Central Political Council, was still in the political wilderness and residing in Hong Kong. The actual control of the National Government was limited to the central provinces, their influence over the North and South depending on the personal relations of Chiang Kai shelp the North and South depending on the personal relations of Chiang Kai-shek with Chang Hsueh-liang in Peking and Chen chi-tang at Canton respectively. The former had definitely thrown in his lot with Chiang Kai-shek, and, while still ruling his Northern fief in the same feudal manner as his father, could be relied upon to lend his full support to the National Government. It was true that Shantung under Han Fu-chu and Shansi under Yen Hsi-shan represented more doubtful elements, but, generally speaking, the stability of the political situation in the North was assured by the young marshal's close relations with Nanking. In Kwantung Chen Chi-tang's position was somewhat different, inasmuch as, while he himself evidently had some private understanding with Chiang Kai-shek, his Administration enjoyed a greater measure of autonomy and adopted generally a much more independent attitude vis-à-vis the Central Government. Moreover, the "South-West Political Council" continued in being and Canton remained the home of the disaffected Cantonese politicians of the Kuomintang, who were continuously threatening to break openly with the National Government at Nanking, and who were only held in check by Marshal Chen and the local military chiefs. Fukien, under the control of Chiang Kuang-nai and Tsai Ting-kai and the XIXth Route Army, occupied politically, as geographically, a half-way position between Canton and Nanking. And in the south-west, Szechuan and Yunnan continued to enjoy full autonomy while recognising the existence of the National Government at Nanking.

- 3. Except for the Fukien rebellion, the disappearance of Chang Hsueh-liang and the extension, in the circumstances described below, of the direct authority of Nanking into North China, the framework of the National Government and its relations with the outlying provinces remain much the same at the end of 1933 as they were at the beginning of the year.
- The end of the year 1932 had seen the ominous gathering of war clouds in North China over the question of Jehol Province, which, under its corrupt old Governor, Tang Yu-lin, a relic and legacy of Chang Tso-lin's régime, had remained for months suspended, so to speak, between China and Manchukuo. It was an open secret that the Japanese intended sooner or later to secure the incorporation of the province into Manchukuo, the extent of which had at the time of its declaration of independence the year before been proclaimed to include Jehol as well as the Three Eastern Provinces; and the Kwantung army authorities had let it be publicly known that any attempt to reinforce the worthless Chinese provincial troops in the disputed territory would be regarded as a hostile act and entail serious consequences. The Chinese were therefore in a dilemma, since they had to choose between sending reinforcements into Jehol and thus precipitating a conflict in North China, or doing nothing and leaving the province the defenceless prey of the Japanese military in Manchuria. In the result the Chinese Government decided that Jehol must be defended, and in the closing days of the year Chinese troops were ordered into the province. In this way Chang Hsueh-liang, in his character of undisputed ruler of North China, found himself in the unenviable position of having to take active steps to defend Jehol Province against the threatened Japanese invasion, and to pit his personal army and the worthless rabble of Northern Chinese soldiery nominally under his orders against the highly efficient war machine of Japan.
- 5. It seemed that the storm was about to burst when Chinese and Japanese forces clashed at Shanhaikuan on New Year's Day 1933, with the result that the Japanese military ejected the Chinese troops and seized control of this important strategic point. The rights and wrongs of this incident will probably never be known, but it suffices to recall the fact that the control of Shanhaikuan was a necessary part of any Japanese plan of campaign in Jehol, and that their right to keep a garrison there for the purpose of maintaining free communication between Peking and the sea under the protocol of 1901 afforded every opportunity for the requisite action.
- 6. On the 10th January the Waichiaopu addressed communications in identic terms to the principal foreign Legations other than the Japanese calling the attention of the Governments concerned to the fact that the Japanese troops had taken advantage of the provisions of the 1901 protocol to occupy Shanhaikuan, slaughter peaceful Chinese citizens and inflict damage to property, and disclaiming all responsibility on behalf of the Chinese Government for any situation which might result from the exercise by the Chinese defensive forces of their right of resistance.
- 7. The Shanhaikuan incident did not, however, precipitate a general conflict, and after the Japanese had consolidated their positions in the city and neighbourhood and the Chinese troops had withdrawn out of actual contact, the uneasy state of armed peace along the frontiers of Jehol was continued for a few weeks longer. In the meantime public attention, both in China and abroad, had become focussed on the Jehol situation through the world-wide publicity given to the question by the proceedings of the League of Nations, with the result that an increasingly bellicose spirit prevailed on the Chinese side. Amongst the most prominent advocates of a policy of armed resistance was Dr. T. V. Soong, the energetic Minister of Finance, who in the middle of February paid a flying visit to the North and proceeded, in company with the young marshal, to Jehol City (Chengteh) to inspect the defences and encourage the Chinese troops. It was, however, significant that Chiang Kai-shek continued to hold himself aloof from the chauvinistic clamour and chose this particular moment to proceed to Kiangsi to direct the operations of the Government forces against the Communists in that province.
- 8. A considerable Chinese army, composed, however, of miscellaneous units, for the most part ill-organised and ill-equipped, had by this time been mobilised [9914]

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for the purpose of taking the field against the Japanese in defence of Jehol. Nor was it long before they were afforded the opportunity of demonstrating their fighting value, which proved to be nil. On the 23rd February the Japanese representative at Nanking handed to the Minister for Foreign Affairs an ultimatum in the form of a memorandum stating that the presence of Chang Hsueh-liang's troops in Jehol was a menace to the peace and order of the province and incompatible with the sovereignty of Manchukuo, but adding that if Tang Yu-lin and the other Chinese leaders in Jehol would surrender to Manchukuo they would be generously treated. At the same time the Japanese columns were set in motion and the invasion of Jehol commenced. The resistance of the Chinese troops in the province collapsed almost at the first onslaught, and within ten days or so a small Japanese detachment entered Jehol City (Chengteh), on the 4th March, while the Chinese forces, converted into a defeated rabble, poured out through the various passes in the Great Wall.

- 9. The Chinese leaders, who seem on occasion to have a genius for doing the wrong thing at the wrong time, after having been ignominiously ejected from Jehol with scarcely a show of resistance, instead of breaking off the battle and withdrawing out of range, now rallied their forces round the gates of the Great Wall, notably at Kupeikou and Hsifengkou, and clung desperately to their positions on these last inches of Jehol territory. Moreover, the public clamour was by this time so great that Chiang Kai-shek was compelled to take action, and two of the relatively efficient German-trained divisions of the National Government were transferred from Honan to the northern front. By the middle of March these Nanking troops were in occupation of the Peking area, while some of their units were already in action with the Japanese at Kupeikou.
- 10. One immediate result of the collapse of the Chinese defence of Jehol, and the consequent intervention of Chiang Kai-shek, was the elimination from the political scene of Chang Hsueh-liang, who had ruled for five years as autocrat in North China since the death of his father, Chang Tso-lin. From the outset Young Chang found himself between the millstones of Japanese aggression and Chinese nationalism, and it was in all the circumstances surprising that he maintained himself so long. Having thrown in his lot with the National Government, the young marshal had had the misfortune to become at one and the same time a thorn in the side of the Japanese and a scapegoat in the eyes of his countrymen, first, on account of the loss of the Three Eastern Provinces and now for the inglorious failure to defend Jehol. In these circumstances, his position became impossible. Early in March Chiang Kai-shek paid a brief visit in his armoured train to the North. After meetings between General Chiang and the young marshal and other northern leaders at Paotingfu, it was announced on the 10th March that the resignation of Chang Hsueh-liang had been accepted, and that the direction of affairs in the North had been temporarily entrusted to Ho Ying-chin, the Minister of War in the National Government, and one of the most trusted supporters of Chiang Kai-shek. Much was to happen before the situation in the North became stabilised, but in the result these events were to lead to the end, for the time being at any rate, of personal "War Lord" rule in North China and to the extension for the first time in the history of the Chinese Republic of the direct authority of the Nanking Government over the Peking and Tientsin area. A few weeks later the young marshal left Shanghai for Europe, where he remained till the beginning of December, when it is understood he sailed for China.
- 11. By the latter part of March the Chinese forces had been finally ejected after severe fighting from Kupeikou, and the Japanese military authorities at Mukden announced that the operations in Jehol had been completed and that the Japanese forces would, unless attacked by the Chinese, confine themselves to the restoration of order in Jehol Province and to guarding the line of the Great Wall. At the same time they, the Japanese, having achieved their immediate war aims, the rounding off of their conquest of Manchuria by the occupation of Jehol, put out peace-feelers through various direct and indirect channels, urging on the Chinese the desirability of negotiating a settlement and letting bygones be bygones.
- 12. Feeling in China continued, however, to run very high, and in spite of the heavy losses they had suffered, the Chinese military leaders persisted in

launching further local attacks on the Japanese, and hostilities continued all along the line of the Wall from Shanhaikuan to Kupeikou. Early in April the Japanese found themselves under the necessity of undertaking considerable operations inside the Wall with the object of driving the Chinese troops away from the frontiers of Jehol. This they had no great difficulty in doing, but no sooner did they start withdrawing again than the Chinese unwisely advanced, claiming, to make matters worse, to be winning great victories over the national enemy.

- 13. These hostilities between the Chinese and Japanese forces in North China continued (without—as in the case of fighting round Shanghai the year before—the existence of any official state of war between the two countries) throughout March, April and May, until the conclusion, in the circumstances related below, of the Tangku Armistice Agreement on the 31st May. In the state of popular emotion prevailing in China, it seemed impossible for any Chinese leader to assume the responsibility of negotiating a settlement or even of ordering a general retirement of the Chinese forces, whose continued resistance was quite ineffective and merely provoked the Japanese to advance further and further into North China. Early in May the Japanese launched a further general offensive, and by the middle of the month the line of their advance had reached Miyun, quite close to Peking, in the North, and a point beyond Tongshan on the railway from Shanhaikuan to Tientsin, in the South. The situation at this period was fraught with grave possibilities, and it seemed as though a Japanese occupation of Peking and Tientsin was imminent. Many rumours were also current of plots amongst Chinese reactionary leaders for the establishment under Japanese protection of an independent Government in North China as a preliminary step towards the extension of Manchukuo to the line of the Yellow River. Japanese aeroplanes dropping propaganda leaflets were paying daily visits to Peking, where a state of panic prevailed. The contents of the palace museum had already been removed to the South, and a general exodus of well-to-do Chinese and students from the local universities set in.
- 14. Amongst the many curious and abnormal features of the situation at this time was the fact that, while the Chinese were fighting desperately and suffering heavy losses in opposing the advance of the Japanese on Peking, a Japanese garrison was all the time permanently stationed inside the city under the protocol of 1901, while Japanese troops travelled unmolested up and down the railway in accordance with their rights of guarding the line and keeping open communications between Peking and the sea.
- 15. It was during this period of extreme tension that His Majesty's Minister was approached by emissaries from both sides with unofficial suggestions for mediation, which, however, led to no results, because the Chinese Government could not at this time screw their courage up to the point of authorising their representatives to make a formal request for peace negotiations.
- 16. In the meantime an important development occurred, when on the 4th May the National Government at Nanking issued a mandate appointing a new governmental organ for the North entitled the "Peiping Political Readjustment Committee of the Executive Yuan," to take over the functions of Chang Hsueh-liang's defunct Administration. As chairman of the new council the Government designated Huang Fu, a former Premier of the old Peking Government and Minister for Foreign Affairs during the early days of the National Government at Nanking. General Huang, who had been educated in Japan and had had special relations with the Japanese in the past, had been in retirement for some years, and his appointment appeared to portend a change of policy on the Chinese side.
- 17. It was not long before these expectations proved justified. Huang Fu arrived in Peking on the 17th May, and secret negotiations were soon after opened with the Japanese military chiefs. On the 23rd May General Huang informed His Majesty's Minister in strict confidence of what was going on, and a week later, on the 31st May, Chinese and Japanese delegates signed the Armistice Agreement at Tangku. The essential point of this agreement was the creation of a neutral zone in Hopei Province inside the Great Wall, which the Chinese troops were not allowed to enter and from which the Japanese army

would retire after satisfying themselves of the Chinese withdrawal. On the whole, in view of the inability of the Chinese to prevent the Japanese from occupying Peking and Tientsin and the whole of North China, the terms of the agreement were not too unfavourable for the Chinese side. The Japanese, on the other hand, while renouncing, for the time being at any rate, all further military aggression in North China, secured all they originally wanted in the form of a demilitarised zone, which guaranteed the frontiers of Manchukud against further Chinese attacks.

- 18. The Tangku Armistice Agreement, which, as subsequent events were to prove, marked a turning-point of the first importance in the relations between China and Japan, was concluded on the instructions of the National Government at Nanking. Chiang Kai-shek himself had throughout, as a practical soldier, realised that China was in no condition to resist by force the Japanese invasion of Manchukuo and Jehol, and he had always favoured a policy of cutting China's losses outside the Wall and concentrating on internal reconstruction and the restoration of law and order and the suppression of the Communist danger in China proper. At the beginning of the year the National Government had been strengthened by Sun Fo's assumption of office as head of the Legislative Yuan, and in the middle of March Wang Ching-wei had returned from Europe and been prevailed upon to resume his post as chairman of the Executive Yuan and therefore civilian leader of the Government. The return of Wang Ching-wei meant a great accession of prestige to the National Government, which was otherwise representative of little beyond the dictatorship of Chiang Kai-shek, and when in due course Wang became converted to the views of General Chiang on the vital question of Sino-Japanese relations, it became possible for the Government, in spite of the continued opposition of T. V. Soong and Lo Wen-kan and other advocates of a policy of no compromise and resistance to the last, to take their courage in both hands and authorise a local settlement with Japan in North China. The situation had, moreover, been further eased by the temporary elimination from the scene of Dr. Soong, who in May had left China on a mission to the United States of America and Europe in connexion with the Economic Conference and other matters. It was in these circumstances that Huang Fu was sent North to make terms with the Japanese, a task which he accomplished, it was generally admitted, with skill and courage.
- 19. On the whole the Tangku Armistice Agreement was well received by Chinese public opinion, which professed to regard it as an unavoidable, if humiliating, step, and was prepared with the similes of France after 1870 and Germany after 1918 as instances of great countries which, having met with disaster, had decided to take their medicine and concentrate their energies on internal reconstruction. As was, however, to be expected, there was an outcry from the South. Eugene Chen had recently returned from abroad to Canton and joined the South-West Political Council, which had issued in the middle of May a manifesto, the English text of which was obviously in Mr. Chen's most scathing style, attacking the Nanking Government under cover of an alleged exposure of their dealings with Japan. This manifesto, addressed to the country at large, the League of Nations, the signatories of the Washington treaties and the Union of Soviet Socialist Republics, alleged that negotiations were being carried on by the Nanking Military Commission with the Japanese General Staff for a settlement under which the Chinese Government, while not recognising the independence of Manchukuo, would check all activities disturbing the peace of the Manchukuo Government as a de facto régime, agree to a neutral zone in the North and give guarantees against the boycott, in return for which the Japanese Government would abrogate the unequal treaties and surrender extra-territoriality, the whole arrangement to lead eventually to a political and economic alliance between the two countries which would extend to the rest of China the system of "co-operation" already worked out by the Japanese General Staff in Manchukuo. In these circumstances the conclusion of the Tangku Agreement was bound to provoke a further storm of protest from the Cantonese politicians, who in June issued in the name of the "South-West Political Council of the National Government of China' another manifesto attacking Nanking and Chiang Kai-shek and denouncing the terms of the armistice. It was, however, generally understood that these hostile demonstrations from Canton

were to be taken at their face value as political gestures, and that, as long as Chen Chi-tang remained in control of the situation in the South, things would not go beyond such paper declarations. The position of the National Government was in any case greatly strengthened $vis-\grave{a}-vis$ the Cantonese politicians by the presence at Nanking of Wang Ching-wei and Sun Fo, two of the most influential leaders of the Southern Kuomintang.

- 20. A more serious reaction to the Tangku Agreement came, however, from the North. Marshal Feng Yu-hsiang was living in semi-retirement at Kalgan, whence he had been issuing statements, in line with those emanating from Canton, taking the National Government to task for their failure to resist the Japanese invasion of Chinese territory. When the news of the conclusion of the armistice became known, Marshal Feng, who had been joined by his former adherent, Fang Chen-wu, and other dissatisfied ex-Kuominchun generals, issued a manifesto denouncing the National Government, proclaiming that he had assumed office as Commander-in-chief of the People's Anti-Japanese Army and calling upon the nation to rise in defence of Chinese territory.
- 21. There seems little doubt that there was a connexion between the protests and threats of secession from Canton and Feng Yu-hsiang's coup at Kalgan; and, in fact, that the latter was intended to coincide with a general hostile demonstration by the Southern leaders against Chiang Kai-shek. It was known that intrigues of some kind had also been going on with the XIXth Route Army in Fukien. Detachments of that army had been preparing to march north with the Cantonese Expeditionary Force, nominally in order to fight the Japanese, but actually, it was suspected, with ulterior motives. It was also not without significance that Chiang Kuang-nai and Chen Ming-shu (the former chief of the XIXth Route Army, who subsequently played an important part in politics at Canton and Nanking) had been in Canton in the first part of June. It seemed, however, that Chen Chi-tang and the other military leaders in de facto control of Kwangtung refused to be party to these plots; so that the coup in the North went off in the air, leaving Marshal Feng and his associates isolated at Kalgan.
- In the meantime, apart from Marshal Feng's movement in Kalgan, the Chinese authorities were also faced, in connexion with the execution of the terms of the armistice, with two other major problems, namely, the resumption of Chinese control over the railway, which from Tongshan to Shanhaikuan was in the hands of the Japanese military authorities, and the restoration of order in the neutral zone. Under the agreement the policing of the demilitarised area was left to the Chinese authorities, but, in addition to the fact that the latter were not allowed to send Chinese troops into the zone, their difficulties were enormously increased by the presence therein of tens of thousands of bandits and irregulars and so-called Manchukuo volunteers, including more especially the forces of the notorious Li Chi-chun. Eventually, after some weeks of negotiations, including early in July a conference at Dairen between Chinese and Japanese and Manchukuo representatives, a general settlement of sorts was reached, both in connexion with the resumption of Chinese control over the railway up to Shanhaikuan and in regard to the incorporation in the special Chinese constabulary for the policing of the neutral zone of a proportion of Li Chi-chun's irregulars and the disbandment of the rest. The result of these arrangements was that a measure of order was maintained along the railway, while a state of general anarchy prevailed in the interior of the zone, the ultimate control of which remained in the hands of the Japanese authorities.
- 23. As the summer advanced it became increasingly apparent that the Tangku Agreement marked a turning-point in the policy of the Chinese Government as regards Sino-Japanese relations, and that the new Administration in North China under Huang Fu was designed to conciliate the Japanese, and to effect so far as might be possible a settlement of outstanding questions in the North, and even to pave the way for the restoration of more normal relations between the two countries. The National Government (that is to say Chiang Kai-shek and Wang Ching-wei) had, in fact, decided to make the attempt to get on terms again with Japan, without compromising their position in regard to Manchukuo, and leaving aside for the time being the Manchurian issue. In reaching this decision the Government was challenging not only their political

opponents in the South, who could be relied upon to make all possible capital out of such a situation, but also those members of the Government itself, such as the Ministers of Finance and Foreign Affairs, who were known to be uncompromisingly hostile to any policy of rapprochement with Japan. The former, Dr. T. V. Soong, was, as stated above, abroad during the summer. As regards the Minister for Foreign Affairs, an unexpected solution was found when towards the end of August Dr. Lo Wen-kan left Nanking by air on a mission of inspection to Chinese Turkestan, the Waichiaopu being taken over by Wang Ching-wei concurrently with his duties as head of the Executive Yuan.

- 24. The independence movement of Feng Yu-hsiang in the Chahar territory of Inner Mongolia dragged on during the summer. The National Government, acting through Ho Ying-chin and Huang Fu in Peking, were, however, able to deal with Marshal Feng's challenge by political manœuvre, and thus avoid any open recourse to force which might have precipitated a civil war. The principal military force in Chahar was represented by the army of Sun Tien-ying, which had been ingloriously ejected from Jehol by the Japanese, and the Government were able to induce General Sun to accept their orders for a nominal transfer of his troops to the Kansu-Kokonor border. As Sun Tien-ying's troops marched out of Chahar into Suiyuan Province, en route for the north-west, the Government forces of Sung Che-yuan, the Governor of Chahar, moved up the railway from Peking towards Kalgan. Meanwhile, negotiations were proceeding with Feng Yu-hsiang, who eventually in the middle of August agreed to throw in his hand, accepted the terms offered by the Government, and left Kalgan to return to his former place of retirement in a temple below Taishan in Shantung, where he is now again living as a private individual under the protection of Han Fu-chu.
- 25. The departure of Marshal Feng from Kalgan was the end of the movement so far as he was concerned, but it was another two months before his chief supporters in the rebellion, Fang Chen-wu and Chi Hung-chang, were finally disposed of. In September these two leaders, with some thousands of followers, finding it increasingly difficult to support themselves on the bleak uplands of Chahar, worked their way South through the mountains, crossed the Great Wall, and entered the neutral zone on the plains of Northern Hopei. In the latter half of September bands of these outlaws suddenly appeared in the neutral zone north of Peking, where they seized Huaijou and other towns and villages, and generally took over control of the countryside.
- 26. These events created further alarms and unrest in North China, and rumours of plots and rebellion were again rife in Peking, where the authorities, being debarred from despatching Government troops into the neutral zone for the suppression of the rebels, could only dispose their forces along the borders of the zone covering the city. During the latter part of September and early October the rebels made rather half-hearted attempts to advance on Peking and fighting took place between them and the Government troops not far from the city walls. As usual, however, such danger to Peking as existed was political rather than military, and in the absence of any sympathetic reaction amongst the other Northern leaders, the movement soon showed signs of collapsing. The rebel forces, being unable to penetrate the lines of the Government troops, sought to break back into the eastern districts of the neutral zone, where, however, they found themselves attacked by the Japanese. Eventually, about the middle of October, the two leaders, Fang Chen-wu and Chi Hung-chang, left their troops either to surrender or disappear. This was the end of the rebellion, but, as usual, the troops of the leaders remained to be disposed of, with the result that most of them went off to swell the bands of brigands in the neutral zone and its hinterland of hills and mountains.
- 27. The liquidation of these local troubles in the North left the field clear for the next stage in the development of China's new policy vis-à-vis Japan, which, as had by now become increasingly clear, involved decisions on the part of the National Government profoundly affecting the whole internal situation of the country. It was also by the autumn increasingly evident that the Government had decided to make a real effort to come to terms with Japan, and in October negotiations were opened by Huang Fu and Ho Ying-chin with the Japanese Legation for a settlement of outstanding questions in the North. These

proceedings were conducted with considerable secrecy, but it was believed that the subject-matter of the discussions included, as well as the retrocession to Chinese control of the gates in the Great Wall, customs arrangements on the Manchukuo-China frontier, resumption of through traffic on the Peking-Mukden Railway, and the restoration of postal communications.

- 28. In the North the attitude of the local Chinese authorities towards the spanese was markedly friendly, not to say subservient; but in Nanking counsels were sharply divided on the subject of these negotiations. Dr. T. V. Soong had returned at the end of the summer from his European tour, and it was evident that the breach between him and Chiang Kai-shek and Wang Ching-wei on the Japanese issue was widening. Matters finally came to a head at the end of October, when Dr. Soong resigned from his concurrent posts of Minister of Finance and Vice-President of the Executive Yuan. Following on Dr. Soong's resignation the opposition at Nanking to the Peking negotiations came to a head, and it seems that instructions were subsequently sent to Huang Fu to break off or at least go slow with his discussions with the Japanese.
- 29. Down to the time of writing (end of November) there have been no further developments in connexion with these negotiations. It is clear that Chiang Kai-shek and Wang Ching-wei desire to pursue a policy of conciliation $vis-\grave{a}-vis$ Japan, and are prepared to negotiate a local, if not a general, settlement; but as soon as they move too fast in this direction, they rouse the opposition of their watchful critics in the country and in the Government itself, and have to slow down the pace again. Dr. Lo Wen-kan returned early in November from his mission to Sinkiang, but, as he was understood to have left Nanking in order to avoid having anything to do with the furthering of a policy of rapprochement with Japan, it is not surprising that he has not so far resumed office as Minister for Foreign Affairs.
- Chiang Kai-shek himself has spent most of the year in Kiangsi directing the operations of the Government forces against the Communists in that province. It will be recalled that considerable progress had been made the year before in the pacification of Central China and the Yangtse Valley by the successful drive against the Communist forces in the Red Lake district of Hupei and in the Middle River region generally. The principal Communist strongholds remaining to be dealt with were those in the interior of Kiangsi and in the wild mountain country on the borders of that province and Fukien and Kuangtung. Large Government forces were accordingly concentrated early in 1933 in Kiangsi with the object, acting in co-operation with the provincial troops of Fukien (XIXth Route Army), Kuangtung (Chen Chi-tang) and Hunan (Ho Chien), of surrounding and crushing the main Communist forces still in the field against the Government. This anti-Red campaign in Kiangsi continued throughout the year, but, considering the magnitude of the effort made by the Government, the results seem to have been singularly meagre. The failure to achieve any decisive success in these operations has no doubt been due, apart from the difficult nature of the country and the spirit of the Communist forces, to the absence of real co-operation between the Government troops and those of the provincial authorities concerned, who have been more concerned with their own positions than with assisting Chiang Kai-shek to overcome the Communists. Indeed, rumours were already current in the Yangtse Valley during the summer that Chiang Kai-shek's plans were not confined to the crushing of the Communists, but aimed also at dealing with other recalcitrant elements in the South. Particularly equivocal in this respect, and in connexion with their participation in the anti-Communist campaign, was the position in Fukien of the XIXth Route Army and its Cantonese chiefs, whose main preoccupation was to return to Canton, where there was, however, no place for them under the régime of their rival Chen Chi-tang
- 31. Chiang Kai-shek's presence in Kiangsi in connexion with the anti-Communist campaign during the greater part of the year led to much coming and going on the part of the Government leaders between Nanking and Nanchang or Kuling. Continuous conferences were, in fact, held throughout the summer months at Kuling, so that this well-known foreign hill station behind Kiukiang began to assume the character of a Government hot-weather resort.

- 32. As regards the internal affairs of the Kuomintang and the National Government, developments during the year have been mainly negative. It will be recalled that amongst the principal resolutions adopted at the plenary session of the Central Executive Committee held at Nanking in December 1932 were decisions to establish, during the year 1933, a National People's Assembly, to advise and assist the Government during the period of tutelage, and to convene in March 1935 a National People's Congress, to discuss and adopt a permane Constitution. In accordance with the terms of these resolutions two committees were set up early in the year, the first to prepare the necessary legislation for the organisation of the People's Assembly, and the second, under the chairmanship of Sun Fo, to prepare a draft of the new Constitution. The above arrangements were, however, subsequently modified when the Standing Committee of the Central Executive Committee on the 30th March resolved that a National Emergency Congress of Kuomintang delegates should be held on the 1st July, 1933, which would decide on the date for the convening of the People's Congress and on the necessity or otherwise of establishing the People's Assembly.
- 33. It is unnecessary to probe at any length into the intrigues and motives underlying these proposals beyond stating that they were designed to strengthen the position of the Government. Strong opposition was immediately voiced from Canton, and the question of the holding of the Emergency Congress continued for some weeks to be a national issue between Canton and Nanking. The next development in this curious game of political manœuvre was the decision reached by the Standing Committee of the Central Executive Committee early in June to cancel the Emergency Congress fixed for the 1st July, and to convene in its stead the regular Fifth National Party Congress on the 12th November. The only result of this new manœuvre was to transfer the force of the Cantonese opposition to the proposed holding of the Fifth National Congress of Party Delegates; and, finally, it was resolved at a meeting of the Standing Committee of the Central Executive Committee on the 28th September to postpone the convening of the latter congress for a period of twelve months. There the position rests at the time of writing; the Emergency Congress has been abandoned, the People's Assembly has been tacitly dropped, the Fifth Party Congress has been fixed for November 1934, and the People's Congress is to be held in March 1935. Meanwhile, the Constitution Drafting Committee has apparently continued at work and a preliminary draft of the new Constitution has already been produced.
- 34. As regards the south-west, the year has been an uneventful one politically in Yunnan, where Lung Yun remains in control as Governor (or rather chairman of the Provincial Government). Yunnan enjoys complete autonomy, but recognises the National Government at Nanking, and General Lung, a typical representative of the modern Kuomintang militarist, has hitherto been a staunch supporter of Chiang Kai-shek. Kueichow has not been so peaceful, owing to the continued friction, and intermittent hostilities between the Governor Wang Chia-lieh and his rival Yu Kuo-tsai. These local troubles have, however, so far had no repercussion beyond the borders of the province.
- 35. In Szechuan, also, the rivalry between the various provincial chiefs has led to a certain amount of civil warfare, and has also had the more serious result of inviting an irruption of Communists into the province from the north-east. These Red bands, the remnants of the big Communist forces broken up in and partly expelled from Hupei the year before, made their appearance, via North-West Hupei and Southern Shensi, in the northern districts of Szechuan in the spring, but were beaten back without great difficulty. In the meantime, however, the rivalry between Liu Hsiang, whose headquarters were at Chungking, and his uncle, Liu Wen-hui, at Chengtu, had again become increasingly acute. These two leaders divided up between them the control over the greater part of the province, and had already come to blows, without any definite decision being reached, the previous year. During the first half of 1933 it became apparent that Liu Hsiang, who enjoyed the special support of Chiang Kai-shek, was preparing to challenge his uncle once more, with a view to unifying the whole province under his rule. After some months of manceuvring for position with the numerous lesser military chiefs, Liu Hsiang finally took the field early in July. The struggle was a short one, and before the end of August Liu Wen-hui had withdrawn from Chengtu and retired to the western marches.

Unfortunately, however, the elimination of Liu Wen-hui did not lead to any definite settlement of the rivalries between Liu Hsiang and Teng Hsi-hou, and the other local militarists, who continued to be preoccupied with their individual intrigues and ambitions. The result was a further and more serious incursion of the Communist forces into the north-eastern districts of the province. In the autumn these Red bands captured Suiting and Chuhsien, and even threatened descend on the river at Wanhsien; and, though at the time of writing the situation is reported easier, it is not yet fully restored.

- 36. It remains, before closing this account of the internal situation in China during the year 1933, to record the declaration of the Independent Government in Fukien. The XIXth Route Army, which forms its military backing, had been transferred in 1932, after the conflict with the Japanese, from Shanghai to Fukien, its chief, Chiang Kuang-nai, having been appointed chairman of the Provincial Government, and its field commander, Tsai Ting-kai, being placed in military charge of the province. Fukien thus passed, to all intents and purposes, under the control of the XIXth Route Army, whose leaders set to work to govern the province and to deal with the brigands and Communists by whom it was infested. Apart from complaints of high taxation, reports of their activities were generally favourable, and they were supposed to be co-operating with the forces of the Central Government in the operations of the latter against the Communists in Kiangsi.
- 37. The XIXth Route Army is a Cantonese force, which won fame under its original Commander-in-chief, Chen Ming-shu, in the anti-North campaign of the Nationalist armies in 1927 and 1928. Later on, Chen Ming-shu became the rival of Chen Chi-tang for the control of Canton. Being ousted by the latter, Chen Ming-shu was taken into the fold of Nanking, and became Minister of Communications in the National Government. In 1932 he fell foul of Chiang Kai-shek and had to retire for a time abroad. Returning to China, he was in Canton, with Chiang Kuang-nai, in the summer of 1933, when Eugene Chen and the Cantonese politicians were denouncing the National Government on account of the Tangku armistice agreement, and was believed to have been subsequently in Hong Kong conferring with Li Chi-shen (Li Chai-sum).
- 38. This was the background when with surprisingly little warning Chen Ming-shu, Li Chi-shen (the ex-Kuangsi leader so long kept under restraint by Chiang Kai-shek at Nanking after the civil war of 1929), Chiang Kuang-nai and Eugene Chen announced, on the 20th November at Foochow, the establishment of an independent Government in Fukien. According to their declarations, the main planks in the platform of this ill-assorted rebel Government appeared to be opposition to Chiang Kai-shek, the Kuomintang and Japan, with a marked tendency towards Leftist, if not Communist, principles.
- 39. In so far as the new movement is directed against Chiang Kai-shek and the allegedly pro-Japanese attitude of the National Government, it follows familiar lines, but the denunciation of the Kuomintang and the adoption of Communist principles give it a more distinctive and possibly dangerous character. It also seems directed as much against Chen Chi-tang as against Chiang Kai-shek, and, inasmuch as the XIXth Route Army and its Cantonese chiefs are the former's rivals for the rulership of Kuangtung, it is fair to assume that the movement represents a rebellion of certain Cantonese elements now out of office, but desirous of regaining control over Kuangtung.
- 40. While, however, Chen Chi-tang is in military control over Canton, and probably has a secret understanding with Chiang Kai-shek, the attitude of the Cantonese politicians, as voiced by the South-West Political Council, may be summed up as disapproval of the new separatist régime in Fukien in so far as its Communist affiliations are concerned, but sympathy with it on what they regard as the "dictatorship" of Chiang Kai-shek. So far, Li Tsung-jen, Pai Chung-hsi and the other Kuangsi leaders have made no open move towards siding with the rebellion, and continue to sit on the fence.
- 41. The Central Government has consequently been placed in a position of considerable difficulty as to the liquidation of the rebellion. Chiang Kai-shek has announced his confidence in his ability to suppress the movement by force, but the Nanking Government generally appear to favour more conciliation

measures. A delegation, composed of Chang Chi and three other prominent members of the Kuomintang, spent the greater part of December in Kuangtung and Kuangsi discussing the situation with the Southern leaders. According to a statement made by the delegation on their return to Nanking, their mission had been successful in that the South-West leaders "realise the importance of internal unity in a time of external aggression and Communist disturbances"; the purpose of the mission had been threefold, namely, to urge the South-West leaders to present a united front with the Nanking Government against foreign aggression, to exchange views regarding the political situation, and to discuss ways for the suppression of the rebellion in Fukien Province. Meanwhile, further conversations are still in progress between Dr. Sun Fo, president of the Legislative Yuan, and Mr. Hu Han-min, the prominent Kuomintang politician, at present living in retirement in Hong Kong, and it is hoped that an agreement will be reached before the convocation of the fourth plenary session of the Central Executive Committee, which has been postponed from the 20th December to the 20th January, 1934.

- 42. No major operations have taken place except for some skirmishes along the Chekiang-Fukien border, but the Central Government have carried out several air raids on Foochow, Changchow, and other important towns in Fukien, inflicting considerable damage. Foreigners in Amoy and Foochow have been requested by the Chinese Government to withdraw for safety to Kulangsu and Nantai respectively, and advice has been given to British subjects to this effect. The attitude of the Chinese navy appears somewhat equivocal, but it would appear that it has reached an understanding with the XIXth Route Army to maintain neutrality, the navy resuming control of the Mamoi forts and dockyard at Foochow and at Amoy, while the port of Santuao will be turned over to the control of the XIXth Route Army.
- 43. Another result of the Fukien independent movement has naturally been to render impossible the fulfilment of the Government's plans for an encircling drive against the Kiangsi Communists, with whom the independent Government in Fukien are reported to have concluded local agreements for non-aggression, if not an alliance of a more formal nature.
- 44. Reviewing the situation at the end of the year one finds the National Government engaged in the delicate task of seeking to maintain a balance between the new policy of rapprochement with Japan and the national anti-Japanese feeling hitherto so sedulously fostered throughout the country. In the North the events of the early months of the year leading to the elimination of Chang Hsuehliang have not been altogether without advantage to Nanking, who have been able to set up in his place a régime at once loyal to the Central Government and acceptable to, or at least conciliatory towards, the Japanese. On the Yangtse the National Government has continued to consolidate its position so that its writ runs at present unchallenged from Shanghai to Ichang. In the South, apart from the recent rebellion of the XIXth Route Army in Fukien referred to above, such influence as may be exercised by the Central Government in the southern provinces continues to be dependent on the measure of goodwill towards Chiang Kai-shek shown by Chen Chi-tang and the other provincial militarists concerned. Internally the fabric of the National Government has been seriously weakened by the resignation from the Ministry of Finance of T. V. Soong, who has been succeeded by H. H. Kung. Dr. Soong has, however, so far retained his post as head of the National Economic Council and has, therefore, not yet drifted into open opposition. Moreover, the National Government, while in actual fact controlled by Chiang Kai-shek, continues to enjoy the prestige afforded by the support of Wang Ching-wei, as head of the Executive Yuan and Acting Minister for Foreign Affairs, and of other prominent party leaders, such as Lin Sen, the President of the Government, and Sun Fo, Chu Cheng, Tai Chi-tao and Yu Yu-jen, the heads of the Legislative, Judicial, Examination and Control Yuans respectively. Hu Han-min, the rival of Wang Ching-wei to the leader-ship of the Kuomintang, is still in retirement at Hong Kong and, while his name has been freely mentioned in connexion with the secessionist Government in Fukien, there has so far been no indication of his being in any way associated with the new movement. As regards the Kuomintang itself, the influence of the party and its organs is undoubtedly decreasing throughout the country and amongst the

Chinese communities overseas. This waning of the Kuomintang has made things easier in many directions, not only in foreign but also in domestic affairs. But the party remains the only basis, other than a Fascist dictatorship, of the Government, and it is difficult to see what, if it disappears, can in the present state of China's political development take its place as the governing and unifying force in the country.

(2) Manchuria.

(a) General.

- 45. The year under review has witnessed the elimination in Manchuria of practically all serious and organised armed resistance to the penetration of Japanese troops, the consolidation of the Japanese position there and the gradual development of "Manchukuo" as an independent State. At the beginning of the year it was only in North Manchuria that the Japanese troops were meeting with opposition. But by the end of January the campaign had been brought to a successful finish. The "volunteers" movement had virtually collapsed and, although lawlessness still continues to present a serious and as yet unsolved problem to the Manchukuo authorities, it has been deprived almost entirely of its political flavour. By February, therefore, there remained only the Province of Jehol for the Japanese to deal with.
- 46. When the independence of Manchukuo was declared in 1931, the declaration included, as well as the Three Eastern Provinces, the additional Province of Jehol, together with parts of Inner Mongolia. It had, therefore, been apparent from the outset that the Japanese intended to incorporate Jehol Province in the State of Manchukuo, of which it constitutes, strategically, an essential flank, whether defensive vis-à-vis Russia, or offensive as regards the domination of North China. For some time the Japanese sought to secure their aims by diplomatic intrigue. But the degree of public attention, both in China and abroad, which became focussed on Jehol rendered the defence of that province the touchstone of Chinese patriotism. The details of the Jehol campaign are described elsewhere in this report, and it suffices to say here that by the end of the spring the Japanese had succeeded in conquering the whole of the province and also securing the resignation of Marshal Chang Hsueh-liang from his position in North China. With the capture of Jehol and the elimination of the young marshal the Japanese had completed the foundation of the Manchukuo State.
- 47. The Manchukuo Constitution, which was promulgated in February 1932, was described in the last annual report and has remained unaltered, but there are constant rumours that it is intended to raise the position of the Chief Executive to something corresponding to imperial status. His Majesty's consulgeneral at Mukden reports that, although the Japanese military authorities remain silent over this question, the local Japanese consulate-general has on occasions made it clear that the idea is by no means dead, although its fruition within the next year or so is most unlikely. One advantage from the Japanese point of view to be gained from the establishment of a monarchy with Pu Yi as Emperor would be the strong support which it would almost certainly receive from the Mongols, and it seems possible that it is the attitude of the latter which may prove the deciding factor in this connexion. Almost all the Ministers in the Manchukuo Government are Chinese, but they wield little or no power, and all the important decisions of policy are taken by their Japanese "advisers." There is, in fact, no doubt that to-day the Japanese are the real rulers of Manchukuo, and the Chinese who hold important positions are little more than figure-heads. The question would seem rather to be whether the power now wielded by the Japanese civilian authorities is not going shortly to be sharply contested by the Kwantung army.
- 48. Banditry continues to present a serious problem to the Manchukuo Government, and strenuous efforts are being made in this direction. Apart from the large number of Japanese troops maintained in Manchukuo, there are also about 120,000 Manchukuo troops, who are being steadily improved by Japanese training and equipment. It is believed that the greater part of the sum earmarked from the national revenue for defence purposes, *i.e.*, approximately £3 million, will be used for the suppression of bandits. Nevertheless, from reports received, it would appear that it will require at least ten years before the bandits are completely eliminated.

- 49. During the past year the numbers of bandits have apparently somewhat decreased, and, as has been explained above, they have practically lost all political character. His Majesty's consul-general at Mukden considers that conditions in the interior are probably not as bad as in 1932, and states that the large distributing oil and tobacco firms report increasing sales in their native agencies. On the other hand, the bandit class have profited considerably by their experience of the past two years and they now operate in small bands only, thus renderic themselves far more difficult to attack successfully. At the close of the summer raids on trains, kidnappings, the looting of villages, &c., were of frequent occurrence. The capture of the three British officers at Newchwang is described elsewhere in this report. His Majesty's consul-general at Harbin states that the situation in North Manchuria is particularly serious. While few cases of banditry have been reported from the districts served by the Chinese Eastern Railway between Harbin and Hsinching, and Harbin and Manchouli, the conditions along the Harbin-Suifenho branch of the railway have been extremely bad. In Harbin itself over 100 cases of armed robbery, often accompanied by kidnapping and murder, have been reported in the local press. The victims have been mostly Chinese, but recently there have been many cases where foreigners have been involved.
- 50. Since the successful outcome of the Jehol campaign considerable progress has been made in the work of the rehabilitation of the Province of Jehol, the administration being in the hands of the Department of Civil Affairs in Hsinking, operating through agents in Chinchow, Chaoyang and Chihfeng, except as regards finance, which, it is understood, is being dealt with entirely by the Central Government. Special attention is being devoted to the question of communications. Surfacing of motor roads is proceeding apace, and four convoys of lorries run weekly from Chaoyang to Chengtehfu. There is also a regular bus service maintained by the Feng-Shan Railway on this route, which has now been extended to Peking. The railway running north from Chinchow has now been extended to Chaoyang. Up to Peipiao it is run by the Feng-Shan Railway, but the new extension is under the South Manchuria Railway, who have provided the rolling-stock. There is also an aviation service from Chengtehfu, which carries air mail, to Mukden four times a week, and an aerodrome has also been laid out for the civil air service. Plans are also stated to be under way for the improvement and extension of the telegraph and telephone service and for the provision of electric light and power.
- 51. Considerable efforts are being made to improve the Manchukuo judicial system. At the end of last year reports appeared in the press that officials in the Ministry of Justice had commenced work on a plan for the remoulding of the Law Court Organisation Law, which would be based largely on the Japanese model, and that, when it had been completed, further steps would be taken to reorganise the prison system and the law governing barristers. In May a press report appeared, to the effect that the Ministry of Justice had decided to ask for an appropriation of 9 million yen in the budget estimate for the next fiscal year in order to facilitate these steps. Closely interwoven with these reforms, which will mainly be based on the advice of Japanese judicial experts, is the question of the proposed abolition of extra-territorial privileges. Discussion regarding this proposal, which at the moment is chiefly confined to the case of Japan, has recently been very much to the fore, but it appears unlikely that any change in the present position will actually take place within the immediate future. The Japanese privileges, which would be surrendered, would, it is understood, include consular jurisdiction, administrative rights in the South Manchuria Railway zone, and such rights and interests as those concerning taxation and business management.
- 52. One of the most prominent features in the financial situation during the last year has been the policy of financial centralisation pursued by the Manchukuo Government and the use of the Central Bank of Manchukuo as its executive authority. The notes issued during the former régime, of which there are said to be fifteen varieties and totalling some 142 million dollars, are now being redeemed by the Central Bank. The new notes issued by the bank are not, however, convertible.

- 53. The most important financial measure taken by the Government has undoubtedly been the stabilisation in April of the currency. The exchange rates of the gold unit and haikwan tael were fixed at the gold unit = 1.95 Mexican dollars, and the haikwan tael = 1.56 Mexican dollars. Discussions have been proceeding for some time past between the Japanese and Manchukuo Governments on the subject of the reform of the Manchukuo currency system, and the sible linking of its unit of currency, the dollar, to the Japanese yen. But no agreement has yet been reached. The proposal to withdraw Japanese bank-notes (gold and silver) from circulation in Manchuria was dropped.
- 54. At the end of June the Manchukuo Government passed for the second fiscal year a balanced budget of 149,169,178 Mexican dollars. In publishing the budget, reference was made to the fact that it had been balanced without resorting to any loan flotation except for the 7 million dollars to be appropriated for constructing State highways.
- 55. At a customs conference in April it was decided to open new branch custom-houses on the Korean border and along the Great Wall as soon as order had been restored in Jehol Province. His Majesty's consul-general at Mukden reports that there has been a marked improvement in the smuggling situation throughout South Manchuria, which he considers is to a great extent due to the effective measures taken by Mr. Fukumoto, Commissioner of Customs at Dairen. Mr. Major states that there is evidence that the Manchukuo customs service is falling more and more under the domination of the Japanese, and that in September it was reported that a further forty Japanese had been taken on as customs officials.
- 56. The revision of the Manchukuo customs tariff, which previously had been similar to that of China, was promulgated in July. It is described in a separate section of this report.
- 57. The Manchukuo Government has declared on several occasions that it intends to adhere to the "open door" principle. In May, in a statement reaffirming its policy in this respect, the Government declared that it was most anxious to secure the financial co-operation of foreign countries in developing the natural resources of Manchukuo. The Government added that it was in no hurry to secure recognition from other countries, but at the same time countries which did afford recognition and could enter into agreement with the Manchukuo Government would obviously occupy a more favourable position than those which failed to do so. British insurance companies have repeatedly complained of discrimination in favour of Japanese firms. No satisfaction has been received as regards the cases that have been taken up unofficially with the Manchukuo Government. As a whole, however, it cannot be said that British trade has, at any rate as yet, suffered to any large extent through the establishment of the present régime, and His Majesty's consul-general at Mukden reports that British oil, rubber, motor car and tobacco firms continue to do satisfactory business.
- 58. At the end of March, after a series of long and tedious negotiations, the British-American Tobacco Company eventually obtained written permission to erect and operate a cigarette factory in the South Manchuria Railway zone in Mukden, which, it is believed, is the first concession of this kind which has ever been granted to foreigners. Negotiations are still continuing as to the exact site of the factory, but there seems reason to hope that this question will soon be satisfactorily settled.
- 59. At the end of last year it was at length announced that the State Council at Hsinking had approved the plan of the commission for the liquidation of claims against the former Manchurian authorities, totalling over 12 million dollars. In accordance with this arrangement, 55 per cent. payments on "category A" claims (i.e., claims for goods actually delivered to institutions, &c., of the former Liaoning Government) have been made to British claimants by the Manchukuo Government. The remaining 45 per cent. due in respect of "category A" claims and the total amount due in respect of "category B" claims will be liquidated by a bond issue, the arrangements for which have been completed. The bonds will carry 3 per cent. interest spread over a period of twenty years, but under the terms of issue claimants will be able to sell their bonds to the Central Bank of Manchukuo at any time for 60 per cent. of their face value.

- 60. Civil aviation in Manchuria has taken a big stride forward during the last year, and a new company under Government control has been formed to take over the management of all Manchurian airways with the exception of the Dairen-Antung air route, which is controlled by the Japan Air Transport Company. Passengers and air mail are carried on all the existing airways. Elaborate plans have been drawn up for road construction in Manchuria, and these include the building of some 60,000 kilom. within ten years at an approximate cost of 90 million yen. The position with regard to the railways is discussed in a separate section. There is still no direct postal communication between Manchukuo and China, and no through communication on the Peking-Mukden Railway.
- 61. At the end of last year the Manchukuo Government passed legislation establishing a State opium monopoly. Central depots were set up for the sale of opium wholesale in the country, each depot having jurisdiction over a specified area, and Government licences were issued to applicants who wished to sell on a retail basis the opium supplied from the depots. At the same time legislation was passed stating that no one was allowed to smoke opium, but that special permission might be given to persons not being minors who had acquired the habit and needed opium for their health. Opium smokers were to have in their possession police certificates. His Majesty's consul-general at Harbin reports that it does not appear that these restrictions are taken seriously, and that the opinion generally held is that the policy of the Manchukuo Government is based on considerations of revenue, and not on any desire to control the production of opium with a view to the eventual eradication of opium-smoking. According to His Majesty's consul-general at Mukden, the cultivation of the poppy has greatly increased in Fengtien Province during the last year.
- 62. In addition to questions connected with the Chinese Eastern Railway, which are dealt with under a separate section, there have been many causes of friction between the Soviet and Manchukuo officials, amongst which figure questions connected with the rectification of the frontier between Manchukuo and Soviet Russia, the alleged encroachment by the Soviet Government on neutral territory at the junction of the Sungari and Amur Rivers, and navigation rights. Further, there have been several troublesome frontier incidents, which have resulted in a number of protests being exchanged between the local Manchukuo authorities and the Soviet consul-general at Harbin.

(b) Railways.

- 63. On the 28th March a conference was held at Harbin to discuss the various outstanding questions of dispute between the Soviet and the Manchukuo Governments in connexion with the Chinese Eastern Railway. The principal matter in dispute was the right of the Soviet Government to retain on their railway system over 3,000 cars and some eighty locomotives claimed by the Chinese Eastern Railway to be their property. Besides demanding the return of the rolling-stock and locomotives, the Manchukuo representatives challenged the right of the Soviet Government to take any Chinese Eastern Railway freight cars, even temporarily, across the Soviet frontier.
- 64. The conference proved abortive, but M. Kuznetsoff, the vice-president of the Railway Board, was reported to have undertaken, on behalf of his Government, to return in due course all the rolling-stock which could be clearly shown to be the property of the Chinese Eastern Railway, and to pay by way of compensation 3 gold roubles a day for each car from the date of entry into Soviet territory to the date of return to Manchukuo. As regards the locomotives, however, he claimed that they were the property of the Soviet Government as successors in title to the Government under M. Kerensky, by whom they had been ordered in 1917 from America. This claim was held to be quite inadmissible by the Manchukuo Government, and they took steps, by closing railway switches, &c., to prevent any more freight cars leaving Manchukuo territory via Manchuli. They supplemented this action on the 12th April by notifying M. Kuznetsoff in writing that his Government would be allowed one month within which to return all the missing rolling-stock and locomotives, and they reserved the right in case of default to take such other measures as they should deem necessary.

- 65. On the expiration of the time assigned, a few cars but no locomotives had been returned, and it was alleged by the Department of Communications that the removal of Chinese Eastern Railway cars to Soviet territory had been continuing in the interval via Pogranichnaya. On the 1st June the through traffic of freight cars from the Chinese Eastern Railway to the Ussuri Railway as stopped by disconnecting the switches between the two railways. A series of protests by Soviet officials followed at Moscow, Tokyo and at Harbin, and M. Kuznetsoff was instructed to suggest that another joint Manchukuo-Soviet conference should be held at Harbin. A few days later it was announced that the Manchukuo Government had no objection in principle to the proposed conference.
- 66. But meanwhile more important negotiations were taking place elsewhere. At the beginning of May M. Litvinov had informed the Japanese Ambassador at Moscow that the Soviet Government would be prepared to consider the sale of their interests in the Chinese Eastern Railway to Japan or Manchukuo. The offer was forthwith referred to Tokyo, and, in spite of the protests of the Chinese Government at Nanking, it was arranged that a tripartite conference should assemble at Tokyo to consider the matter, and the conference, attended by Manchukuo and Soviet representatives, together with Japanese "observers," opened on the 26th June.
- 67. The Japanese Minister for Foreign Affairs, who opened the conference, stressed the fact that its scope would be limited to commercial negotiations. At the beginning of the conference the Russian offer for the sale of their rights in the line was 250 million gold roubles, which, at the rate of exchange then prevailing, amounted to about ten times as much as the Manchukuo Government were prepared to pay. Moreover, while the Soviets maintained that they had complete ownership of the railway, Manchukuo were only prepared to admit Soviet's claim to half-ownership in the line. The Soviet Government have since reduced their price, which still remains, however, almost twice as large as what the Manchukuo are prepared to give, and at the time of writing a complete deadlock appears to have been reached.
- 68. While these negotiations were proceeding the Harbin police arrested, on the instructions of the Manchukuo Government, four important Soviet officials of the Chinese Eastern Railway. No official announcement was made of the charges preferred against them, but it was emphasised that the proceedings were of a purely legal character having no political motive whatever. On the same day the stationmaster at Manchuli and Suifenho (both Soviet citizens) were sent under escort to Harbin to be examined by the procurator. The situation was complicated by a dispute as to who was to discharge their duties during their detention. The Soviet general manager of the railway appointed four Soviet citizens to act temporarily for the detained officials, but the Manchukuo Government contested these appointments as ultra vires, and maintained that the respective assistants of these officials (Manchukuo citizens) should automatically replace them during their absence. An acrimonious discussion is thus proceeding, and the rival acting officials each claim the right to take charge of their respective offices. The Soviet consul-general at Harbin has made repeated representations to the local Manchukuo authorities against the arrest of the Soviet officials.
- 69. An agreement was concluded in March between the Manchukuo Government and the South Manchuria Railway Company by which the latter assumed control of all railways in Manchuria with the exception of the Chinese Eastern Railway and established a Railway Control Board in Mukden. Subsidiary bureaux have been set up at Taonan, Kirin and Harbin. As regards railways in which other Powers are interested financially, the repayment of the loans will be undertaken by the South Manchuria Railway, and under a separate agreement the control of the railways in North-Eastern Korea has also been handed over to the company. By the unification and co-ordination of the whole system of railways, except for the Chinese Eastern Railway, great economy will, of course, be effected, and it is hoped that capital will be obtained on easier terms. Many rumours have recently been in circulation regarding plans which are under consideration for the reorganisation of the South Manchuria Railway Company, the most important of which is the placing of the company under the direct

control of the Commander-in-chief of the Kwantung Army. There is reported, however, to be strong opposition on the civilian side to this proposal.

- 70. The company's balance sheet for the financial year 1932–33 would appear superficially to be very satisfactory, but, owing to the uncertainty of the financial relationship between the company and the Manchukuo State Railways, which it has taken over, and in view of the large outlays which the company herecently made on enterprises of every description, which can scarcely be expected to bring in any return for some years, it is almost impossible to gauge accurately the real financial position. This may perhaps be more clearly revealed in next year's balance sheet. It is certain that traffic receipts, both for passengers and freight, must have considerably increased during the past year.
- 71. By far the most important development has been the completion of the Hsinking-Tumen Railway, which was formally opened to traffic on the 1st September. The railway includes the Hsinching-Kirin, the Kirin-Tunhua and the Tunhua-Tumen railroads, and its management has been entrusted to the South Manchuria Railway Company. Rashin has been selected as the terminal port of the railway and an ambitious harbour construction plan to be completed in 1947, which will include inter alia the building of a tunnel between Rashin and Yuki, has been started by the South Manchuria Railway Company under contract with the Japanese Government. The importance of the railway is the considerable reduction, with all the consequences resulting therefrom, of the distance between North Manchuria and Japan. It is calculated that the distance between Hsinking and Japan will be reduced by from 500 to 800 kilom. The line will doubtless become a serious rival to the Chinese Eastern Railway, and it seems probable that, when Rashin is fully developed—and it is calculated that this will take some fourteen years—the route is bound to affect Dairen adversely. While Dairen would appear better suited than Rashin for exports to and imports from countries other than Japan, the latter port is likely in due course to be the most used for the transport of goods between Manchukuo and Japan.
- 72. The Lafa-Harbin Railway has now been completed, and the line was opened to traffic in the middle of September. It is also reported that the construction of the new bridge across the Sungari River has been finished. The Harbin-Hailun line has been extended as far as Peianchen. The Tsitsihar-Peianchen through Koshan and Taianchen has been completed, and the Tsitsihar-Laha line has been extended northwards from Laha to Noho. A railway, it is also reported, is being built from Tumen to Hailin, which will serve as a feeder to the Hsinking-Tumen line, and which eventually is to be continued into the region north of the Chinese Eastern Railway.

(3) Mongolia.

- 73. The Japanese, from their base of the semi-autonomous Mongol Province of Hsingan in Manchukuo, have continued their efforts begun in 1932 to win over the Mongols as an effective screen between Russian and Japanese spheres and between China and Manchukuo. The Chinese Government, on the other hand, have at last realised the necessity of counteracting, if possible, the danger of alienation of the Mongols from their fealty to China, and have been developing a policy of bidding for their support by conciliatory gestures, and the offer of attractive political, educational and economic inducements. They have concentrated their efforts in the dissemination of propaganda by means of personal contact with and tactful handling of the feudatory and spiritual leaders of the Mongolian communities, and the diffusion of the tenets of the Kuomintang through selected agents.
- 74. Authoritative confirmation as to the extent to which either side has succeeded in winning the Mongols to their cause is singularly lacking, but from the information actually available, it would appear that the Mongol inhabitants of the North-Eastern Provinces, including Jehol and Chahar, have on the whole reacted favourably to Japanese approaches. The Chinese authorities have given much prominence to protestations of loyalty to the Central Government on the part of the Mongols, but these assertions have to some extent been disproved by recent developments, and early in the autumn it transpired that there was in

movement an organisation under the Silingol chieftain, Prince Teh, to obtain autonomy.

- 75. The Chinese Government, who were at first inclined to make light of this agitation, finally, in the beginning of October, appointed a Government "Goodwill Mission," under the leadership of General Huang Shao-hsiung, the Minister of the Interior, to negotiate with the Mongol leaders. The mission arrived at Kueihua at the end of the month, and spent the following few weeks in negotiations to persuade the Mongols to accept in the place of the very wide measure of autonomy, which they were demanding, some palliative scheme whereby some of their grievances would be met, while the authority not only of the Central Government but also of the Provincial Government would be maintained.
- 76. After protracted negotiations, Prince Teh agreed to abandon his proposal to establish a separate autonomous Government, while the Central Government receded from its original standpoint, namely, to make no administrative changes, but to set up under the jurisdiction of the Provincial Governments of Suiyuan and Chahar special committees composed of Mongols to deal with matters affecting their interests. The tentative compromise stated to have been reached, which still awaits the approval of the Central Government, embodies general principles, under which two autonomous areas, or chu, are to be demarcated in Inner Mongolia, including parts of the provinces of Chahar, Chinghai (Kokonor) and Ninghsia. These areas will be directly under the Central Government. Details of the agreement are at present lacking, but it is understood that, at the same time, there will be changes in the organisation of the Mongolian and Tibetan Affairs Commission at Nanking, which is now the competent Central Government organ.
- 77. General Huang left Kueihua early in December, and proceeded to Nanking, where he reported on the results of his mission. It has not yet been possible to discover whether the agreement will satisfy the wishes of the Mongols, but it has already been denounced as contrary to the spirit of self-determination of the Mongol people.

(4) Sinkiang.

- 78. The revolt of the Tungan leader, Ma Chung-ying, in the Hami neighbourhood, mentioned in the annual report for 1932, proved the prelude to far more serious disturbances in Sinkiang 1933. To assist towards a better understanding of what has been happening in these remote regions of Central Asia, it may be noted that the population of Sinkiang consists of—
 - (a) The Turkis (Chinese Chantou), who are the native Turkish-speaking Moslem population; they are agriculturalists, and live in the scattered oases in the desert. Allied to these Turkis are other native pastoral tribes, such as the Kirghis, who are nomad Moslems and live in the hills and mountains.
 - (b) The Tungans, who are Chinese-speaking Moslems of debatable origin; they are settled in Kansu and in patches throughout Chinese Turkestan, are probably the most virile element in the population, and were largely responsible for the great Mahometan rebellions of the sixties.
 - (c) The Chinese, who are mostly officials and merchants from China proper.

In addition to the above three main elements in the population, who have played the more important part in recent events, there are also in Northern Sinkiang, Kazaks, Kalmuks, Nogais and Mongols, as well as colonies of Russians and Manchus, the latter a relic of Chien Lung's campaigns. The Chinese Administration has for years been the merest veneer, with little or nothing behind it, but the traditions of the past, and ever since the abdication of the Manchu Dynasty, the shadow of another great Mahometan uprising has lain over the country from Kansu to Kashgar.

79. Chinese Turkestan is divided by the Tien Shan into two distinct regions, Northern and Southern Sinkiang, and, owing no doubt to the great difficulties of communication across the intervening mountains and deserts,

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political events during the year have developed along different lines in these two areas. As regards Southern Sinkiang, full information has been available from the reports of His Majesty's consul-general at Kashgar. In the case of Northern Sinkiang, however, information has been scanty, and derived for the most part from Chinese press and other chance reports.

- 80. Dealing, firstly, with Northern Sinkiang, the troubles appear to hav started again early in 1933, when the Tungan leader, Ma Chung-ying, resumed operations against the Chinese provincial authorities in the Hami district. The rebel movement met with little resistance, and soon spread to Urumchi (Tihua), the provincial capital, which was attacked in February. The Tungans were, however, repulsed with the assistance of White Russian mercenaries. Confused hostilities between the various factions continued, until in April some Chinese troops from Manchuria, a portion of the Chinese forces expelled from the Three Eastern Provinces by the Japanese the previous year, who had found their way into Northern Sinkiang, took charge of the situation. The Governor, Chin Shu-jen, whose corrupt and inefficient régime was held in large measure responsible for the outbreak of the revolt, fled, and a new Provincial Government was established under two Chinese generals Liu Wen-lung and Sheng Shih-tsai, as provisional Tupan and acting chairman. In this way a Chinese administration of sorts continued to function in Northern Sinkiang. No settlement of the dispute with Ma Chung-ying had, however, been reached, and intermittent hostilities between the Chinese authorities at Urumchi and the Tungan forces in the Turfan and Hami districts continued throughout the year. Only a minor part seems to have been played in these troubles in Northern Sinkiang by the Turkis, who constitute a less important element in the population in those parts.
- 81. In Southern Sinkiang (Kashgaria) the rising seems to have developed along different lines and to have been largely a revolt of the Turki population against the Chinese and the Tungans. At the outset the Turkis and the Tungans were both operating against the Chinese, and all vestige of Chinese official authority was soon swept away. Khotan, Kerija, Yarkand and other cities in Southern Sinkiang fell successively into the hands of the rebels, the Chinese officials being murdered or deposed, and in May the Old and New Cities at Kashgar were captured, the former by Kirghiz and Turkis and the latter by Tungans.
- 82. The story of these and subsequent developments at Kashgar is too long and involved to recount, but the upshot was that the Turkis and the Tungans soon fell out, leaving the Tungans under Ma Chan-tsang besieged by the Turkis in the New City at Kashgar. In spite of constant attacks by the Turkis and Kirghiz, throughout the summer and autumn Ma Chan-tsang and his Tungans have so far proved too tough a nut for their opponents to crack, and at the time of writing (end of November) they are still holding their own in the New City. Apart, however, from this Tungan force besieged in the New City at Kashgar, the whole of Southern Sinkiang is in the hands of the local Turki population.
- 83. It should be explained that the New City at Kashgar, which lies a few miles from the Old Town, is in the nature of a Chinese fort or cantonment for the accommodation of the Chinese garrison in the old days. His Majesty's consulategeneral is situated in the Old City, which is the real town of Kashgar. It is noteworthy that His Majesty's consul-general and his staff, the Russian consular establishment, and the Swedish mission have not been molested, and that British consular mails have been coming and going between Kashgar and India without interruption throughout the year.
- 84. So far as the available information goes, the movement is not so much a concerted rebellion against the Chinese Government as a rising of the various elements of the native population against the local Chinese officials, whose mandate of government was completely exhausted; and the native leaders, whether Turki or Tungan, continue, it seems, to profess a nominal allegiance to Nanking.
- 85. To revert to the situation in Northern Sinkiang, the Chinese Government in June despatched a Special Pacification Commissioner, General Huang Mu-sung, to Urumchi. General Huang's mission was a failure, and he appears to have become involved in a plot against Liu Wen-lung and Sheng Shih-tsai, with the result that he had to beat a hasty retreat, narrowly escaping with his life.

- 86. The next effort by the Central Government was the despatch (in the circumstances described above) of Dr. Lo Wen-kan, the Minister for Foreign Affairs, on a mission of inspection to Sinkiang. It should be mentioned that these missions were rendered possible by the enterprise of the Sino-German Eurasia Aviation Corporation, which, with the object of ultimately establishing a transcontinental air route to Europe, has been operating, if somewhat intermittently, an air service from Shanghai via Lanchow and Hami to Urumchi. Dr. Lo left Nanking at the end of August by air and duly reached his destination. After meeting Liu Wen-lung and Sheng Shih-tsai at Urumchi and Ma Chung-ying at Turfan, he continued his journey to Chuguchak and returned to China by the Siberian Railway, after an absence of a little over two months. Dr. Lo was, by all accounts, well received by the various leaders in Northern Sinkiang, but his mission appears to have been a fruitless one, seeing that hostilities have since been resumed between Ma Chung-ying and Sheng Shih-tsai.
- 87. To sum up the situation towards the end of the year, so far as it is known to His Majesty's Legation: In Southern Sinkiang Chinese official authority has completely disappeared and the local Turki leaders are generally in control of affairs in the various oases, with the exception of the New City at Kashgar still held by Ma Chan-tsang and his Tungans. In Northern Sinkiang the Chinese leaders, Liu Wen-lung and Sheng Shih-tsai at Urumchi and Chang Pei-yuan in Ili, are still maintaining some sort of Chinese Administration, but are carrying on intermittent hostilities with the Tungan leader Ma Chung-ying, who controls the Turfan and Hami regions.
- 88. It may be added that Chin Shu-jen, the ex-Governor, who made good his escape from Urumchi in the early summer, is reported to have been arrested since his return to China and to be awaiting trial on charges of treason (in connexion with the trade agreement which he concluded with the authorities of the Union of Soviet Socialist Republics in 1931) and general official malfeasance.

(5) Tibet.

- 89. It will be recalled that the Tibetan question, which in its more recent and local phases has been the question of the frontier between China and Tibet, slumbered from 1918, when as the result of local negotiations with British mediation a provisional frontier line was laid down, until 1932, when following on the resumption of local hostilities on the frontier the Tibetans were driven back to the line of the Yangtse. The question having thus been again brought into prominence, representations were on several occasions in 1932 made by His Majesty's Chargé d'Affaires to the Chinese Government, who, while adopting the traditional attitude that the dispute was a purely domestic one, in which His Majesty's Government in the United Kingdom had no right to interfere, professed to have issued orders to the attacking Chinese troops to stay their advance. Whether as the result of these representations, or because of the outbreak of fresh civil war in Szechuan, hostilities on the frontier were, in fact, soon after suspended.
- 90. Early in January 1933 the Dalai Lama, who had evidently been much disturbed by the events of the previous year, addressed a message to the Government of India informing them that he had received from his representative in China a report stating that the Chinese Government were pressing for the negotiation of a settlement without British mediation and were preparing to renew hostilities in case of Tibet's refusal to negotiate. Commenting on this report, the Dalai Lama stated that the Tibetan Government proposed to persist in their request to the Chinese Government to conclude the Simla Convention of 1914 with the aid of His Majesty's Government as mediators. His Holinese also asked that continued pressure might be brought to bear on the Chinese Government to induce them to agree to such tripartite negotiations, and requested the advice of His Majesty's Government as to his future course of action.
- 91. After full consideration by His Majesty's Government of all the issues involved, the Political Officer in Sikkim was in March instructed to send a reply to the Dalai Lama reminding His Holiness that, as the result of the representations made to them by His Majesty's Government the Chinese Government had

stopped the fighting on the frontier, assuring him that His Majesty's Government were anxious to do all they could to assist in finding a permanent solution of the frontier difficulties; but explaining that, owing to the political situation in China, the time was not opportune for pressing the Chinese Government to enter into general negotiations for confirmation of the Simla Convention of 1914. The Chinese Government, the message continued, not being at present prepared to agree to the mediation of His Majesty's Government, pressure on them to accept such mediation would be unlikely to bear fruit. Should the Dalai Lama decide in these circumstances to accept the Chinese offer of direct negotiation on the frontier question, His Majesty's Government would follow the course of the discussions with great interest, and would, of course, be glad if they were to lead to a settlement satisfactory to Tibet. The message concluded with an offer of further diplomatic assistance to induce the Chinese Government to conclude an agreement in the event of the Tibetan Government deciding to enter into such direct negotiations and any proposal acceptable to them emerging therefrom.

- 92. This exchange of messages with the Dalai Lama was of particular importance in view of the attitude adopted by His Majesty's Government in the United Kingdom towards the possibility of direct negotiations between China and Tibet, that is to say, His Majesty's Government while continuing to offer the Tibetan Government their friendly advice and diplomatic assistance vis-à-vis the Chinese Government raised no objections to such direct negotiations, should Tibet decide to enter upon them. The Dalai Lama's reply to the message from His Majesty's Government was dated the 27th March, and, while vaguely worded, appeared to indicate that Tibet was prepared to enter on direct negotiations with China. So far as is known nothing has yet resulted in the matter, the Chinese Government being probably too preoccupied with other and more pressing internal and external affairs to devote serious attention to a settlement of their difficulties with Tibet.
- 93. In spite of many rumours of military movement by both sides, the situation on the Chinese Tibetan frontier seems to have remained fairly quiet during the year. Definite information in regard to the conclusion of local armistice agreements has been lacking, but it seems that the troops of both sides have refrained from crossing the line of the Yangtse, which thus remains the provisional de facto frontier following on the resumption of hostilities in 1932.
- 94. There has been no occasion for formal representations to the Chinese Government on the subject of Tibet during the year, but when His Majesty's Minister was in Nanking early in February he mentioned the situation on the frontier in conversation with the Minister for Foreign Affairs, pointing out that as neighbours of Tibet the Government of India were interested in seeing peaceful conditions maintained therein, and could not acquiesce in Chinese troops entering the country, nor tolerate any action likely to cause disturbance or lead to trouble there; in fact, while His Majesty's Government had no ulterior motives, they strongly objected to any sort of military operations in Tibet. Dr. Lo received these remarks in good part and replied that he quite understood, that there was no desire whatever on China's part to make trouble, and that orders had already been sent to stop the fighting.
- 95. No material progress has been made during the year in the matter of the reconciliation between the Dalai Lama and the Tashi (Panshen) Lama and the latter's return to Tibet. The original of the Dalai Lama's letter to the Tashi Lama urging his Serenity's return to Tibet, was delivered through the agency of His Majesty's Legation to the Tashi Lama at Nanking on the 20th January. The Tashi Lama's reply, which was non-committal, but friendly, and stated that he was sending his delegates to offer gifts and represent matters to His Holiness, was received by His Majesty's Legation on the 4th February, and immediately despatched to the Government of India for transmission to the Dalai Lama. The Tashi Lama's representatives left China for India and Tibet a few weeks later. The Political Officer in Sikkim met them at Kalimpony in the middle of April, when they informed Mr. Williamson that their instructions were to confer with the Dalai Lama and try and persuade His Holiness to adopt a friendly attitude towards the Tashi Lama, so that the latter might be able to return to Tibet. The latest news is that discussions with the Tashi Lama's representatives took place

at Lhassa during the summer and autumn, but that no settlement was reached; and the prospects of the early return of the Tashi Lama to Tibet were then considered to be still remote.

- 96. The Tashi Lama himself returned from Nanking to the North in February, and has spent most of the year in Inner Mongolia, at or near the monastery of Pailingmiao, not far from Kueihuacheng.
- 97. Mr. Williamson, who succeeded Colonel Weir as Political Officer in Sikkim, visited Lhassa, on the invitation of the Dalai Lama, during the summer.
- 98. News has just been received that the Dalai Lama died on the 17th December. It is as yet too early to judge what reactions his death will produce.

(6) Communism.

- 99. The Communist situation in China remains substantially the same as at the beginning of the year. While there undoubtedly exists over the whole country an underground Communist movement of considerable proportion, open Communist activities are confined to the Southern and Central Provinces. The main Communist area is in the Kiangsi–Fukien district. In addition the southwestern region of Hupeh and the hilly country on the borders of Honan, Hupeh and Anhui must be regarded as Communist-ridden. The remaining part of Hupeh, owing to the success of Chiang Kai-shek's campaign in the autumn of 1932, has been more or less reclaimed by Government troops, but the Communists driven out by this campaign have fled into Szechuan via Shensi, and there has, in consequence, been a recrudescence of communism in the north-east corner of Szechuan.
- 100. It is doubtful whether the inhabitants of the infected areas are convinced Communists, and it seems probable that they have temporarily been driven to communism by the misgovernment of the local officials. While the Nanking Government has apparently in theory realised the importance of the economic side of the problem, they have in practice only attempted to solve it by military tactics, which, as is described in the military section of this report, have so far proved unsuccessful.
- 101. During the first quarter of the year, while General Chiang Kai-shek's attention was occupied by developments in the North, the campaign against the Communists was proving disastrous to the Government troops, who lost no less than 10,000 men and 3,000 wounded. As a result a conference was held at Kuling towards the end of May, when a plan of campaign was evolved by which the Communists were to be gradually encircled and starved out. It was then proposed to make raids into their territory with mutually supporting flying columns. The first part of the plan was put into operation shortly afterwards. It was probably as a result of the effect which the campaign was having that at the end of the summer the Kiangsi Communists advanced to a considerable extent into Fukien, practically reaching Yenping, in order to obtain provisions and supplies.
- 102. The main drive by General Chiang Kai-shek, which has continually been reported to be imminent, has been constantly deferred, until it seems likely that it may after all be General Chiang's intention to pursue merely a policy of attrition and steady encroachment on Communist territory. General Chiang has throughout been hampered by the lack of whole-hearted co-operation between the troops of the Central Government and those of the provincial authorities concerned, and recently far more seriously by the Fukien independence movement.
- 103. The situation on the Shensi border in North Szechuan was aggravated at the beginning of October, when the Communists, taking advantage of the renewed civil war, made a raid southwards and caused considerable and somewhat undue alarm at Chungking and Wanhsien.

(7) Nanchang Kidnapping Case.

104. On the 29th March Messrs. Butterfield and Swire's steamship Nanchang was anchored at the mouth of the Liao River off Newchwang, when she was attacked by pirate junks and four British officers, Messrs. Johnson, Hargrave, Blue and Pears, were taken captive. Mr. Vice-Consul Clarke proceeded to the

scene from Mukden to take charge of the case. From the outset, apart from local action at Newchwang and strong representations to the Japanese and Manchukuo authorities at Mukden and Changchun, constant pressure was placed by His Majesty's Embassy at Tokyo on the Japanese Government, who were alone in a position to take effective measures and were considered responsible for the safe release of the captives. It was made clear from the beginning that there would be no payment of ransom by the British side.

105. On the 3rd April one of the captives, Mr. Pears, was released and reported that his companions were being kept in junks in the Panshan area. Communications were immediately established through intermediaries. At the end of April Captain Obata, chief of the Japanese gendarmerie at Newchwang, took effective charge of the case. Some months passed during which the Japanese carried out their negotiations and devised various methods for the release of the captives. In June, with a view to facilitating early release, Butterfield and Swire agreed to guarantee up to 10,000 dollars for expenses provided that the payment was not considered a ransom. Later, this guarantee was increased to 20,000 dollars. Although the Japanese Government, contrary to the assurances given by Captain Obata, endeavoured, at the last moment, to increase still further the contribution from British sources by 20,000 dollars, the matter was eventually settled to our satisfaction and on the 8th September the captives were released and handed over to Mr. Vice-Consul Clarke at Newchwang. It is understood that the brigands received 50,000 dollars, apart from what was paid to the intermediaries. In any case, only 20,000 dollars was paid by the British side for expenses.

(8) Military Operations.

Sino-Japanese Operations.

106. In the autumn of 1932 the Japanese made it abundantly clear that given any excuse they would terminate the volunteer activities in Manchuria and add Jehol to the Three Eastern Provinces. They hoped to secure the allegiance of the Chinese Governor Tang Yu-lin by offering him attractive terms to join the new State, but declared that should the Chinese send regular troops into the province to secure their hold they would regard it as an act of war. In accordance with a resolution of the Military Council Chang Hsueh-liang moved four divisions across the frontier during the last days of December, and on the 1st January, 1933, the Japanese attacked Shanhaikuan with the permanent detachment under Major Ochiai, assisted by tanks and covering fire from naval guns off the coast.

107. Chang Hsueh-liang was now faced with the choice either of a withdrawal of his four divisions, which entailed political extinction, or of the mobilisation of his forces, which would involve a virtual state of war with Japan. He accepted the challenge and began his concentration for the defence of Jehol immediately.

108. By the 15th February some 200,000 men were concentrated from Chihfeng to Chinwangtao and an elaborate defence scheme prepared by German advisers was adopted. The mountainous nature of the country was all in favour of the Chinese, and a few resolute battalions could have delayed the Japanese advance for weeks. The plan adopted necessitated competent staffs for the four armies concerned and co-ordination far beyond the powers of the executants. At the moment of the attack all was chaos, commanders who should have been at the front were in Peking, subordinates had no orders from higher formations, troops were, in some cases, over 100 miles from their positions of readiness and no proper staffs were in existence. Medical and supply arrangements, non-existent during the concentration period, were being feverishly organised only a few days before the blow fell. The moral of the troops was poor, and they were an easy prey to panic when faced with armoured cars and aeroplanes against which they had no defence.

109. The Japanese plan was bold to the point of rashness, but they were evidently well-informed of the opposition they were likely to encounter. Their hardest task was the concentration. In bitter weather, against blinding snowstorms, the 6th and 8th Divisions moved against Kailu and Peipiao respectively,

whilst the 14th Mixed Brigade advanced from Suichung towards Lingyuan. The 4th Independent Cavalry Brigade accompanied the northern column. On the 26th February Chaoyang was captured by the 8th Division, and a mechanised column consisting of two armoured cars and some lorries was organised for a rapid dash on Chengtehfu. This column left Chaoyang on the 1st March and co-ordinated its move to arrive at Lingyuan with the main body of the 14th Brigade. Within three days Chengtehfu was in the hands of the Japanese, and the remainder of the campaign consisted of sweeping the demoralised remnants of the young marshal's troops out of the province. No effective resistance was offered, and the Japanese battle casualties were excessively light. Up to the moment no real assistance had been given by the Nanking Government to the young marshal, but as his troops came pouring pell-mell through the Kupeikou Pass four divisions of Southern troops under Hsu Ting-tao were despatched to guard against a threat to Peking, and Chiang Kai-shek himself came north as far as Paotingfu, where he had an interview with the young marshal and accepted his resignation. The miserable débâcle in Jehol aroused indignation throughout the country, and T. V. Soong was most outspoken in condemning the obsolete methods of the Northern generals.

Four Southern divisions undertook the defence of Peking to check any advance of the Japanese from Kupeikou, although the latter showed no signs of advancing beyond the Wall, and were fully occupied in cleaning up the remnants of Chang Hsueh-liang's forces in the northern and southern parts of Jehol. A certain amount of fighting, which took place at Hsifengkou and the passes to the east, was seized upon in the Chinese press and magnified into victories as evidence of military superiority over the Japanese. The impression conveyed was that, with the arrival of Chinese regular troops, the heroic exploits of the XIXth Route Army would be repeated, and the Japanese would find a further advance too costly to be undertaken. The Japanese soon sickened of these bombastic reports, and determined to demonstrate their military superiority and clear the passes in the Wall of the perpetual menace of raids and sniping. With the aid of a pro-Manchukuo detachment under Li Chi-chun, stiffened with regulars, they struck at Shihmenchai on the 1st April, and chased the Chinese west of Chinwangtao. This operation effectually removed all Chinese troops from the salient, but, in the withdrawal of the column from Haiyang, the troops of Ho Chu-kuo reoccupied the town, and a victory over the Japanese was duly acclaimed by the press. The Japanese had no intention of letting the prowess of their army be challenged in any respect, and staged a still larger operation to drive all Chinese troops east of the Luan River by means of a direct drive along the railway, assisted by columns operating from the passes between Lengkou and Hsifengkou. At the same time they determined to show the Southern troops in the Kupeikou salient that they were no more invincible than the north-eastern armies. To this end they increased their artillery, and started shelling them out of their positions close to the Wall, consolidating the ground won with their infantry as the Chinese retreated under artillery and aeroplane attacks. Having chased the Southerners from their dominant position on the Nantienmen and driven every Chinese regular west of the Luan River, on the 27th April the Japanese again withdrew to the passes in the Wall, and the 27th April the Japanese again withdrew to the passes in the wan, and informed the Chinese very clearly that they would brook no reoccupation of that area. Unfortunately, their warning fell on deaf ears. As each local authority reported the coast was clear, patrols were sent forward, and each city reoccupied was claimed as a victory over the invaders. The Japanese consequently determined to demonstrate their superiority once and for all

111. The Japanese preparation for the attack, which was launched on the 7th May, involved the concentration of the 14th (Hattori) Mixed Brigade at Shanhaikuan, from which a mechanised force of 150 lorries took the route of the old mandarin road. A brigade of the 6th Division was detailed to attack Chienan from Lengkou, whilst a second brigade of this division, emerging from Hsifengkou, moved on Tsunhua. In addition to the regular Japanese forces, Li Chi-chen, with his pro-Manchukuo troops, advanced from Chinwangtao along the railway line. Simultaneously, the 8th Division at Kupeikou began methodically to destroy the four Southern divisions opposed to it by frontal attacks, well prepared by artillery fire and assisted by aeroplane

bombing. To enhance the moral effect, Peking was visited daily by Japanese aeroplanes, which scattered pamphlets of propaganda.

- 112. In about a fortnight the Chinese capitulated. The Japanese, by that time, had destroyed the *moral* of the Southern troops, and had driven the old north-eastern armies like sheep to the line Tungchow-Lutai. The Southern troops had evacuated Miyun, and the threat to Peking was so serious that the Chinese not only realised, but admitted, that further resistance was useless Huang Fu, whose personality was not objectionable to the Japanese, was sent north to take charge of negotiations, and an armistice was signed at Tangku on the 31st May. By its terms, all Chinese troops were to be withdrawn west of the line Yenching-Changping-Shunyi-Tungchow-Lutai. The demilitarised zone thus created could not be entered by Chinese troops. Questions concerning the administration and policing of this zone were a constant source of friction. The Japanese insisted that the bulk of the special gendarmerie slould consist of their late allies, the pro-Manchukuo army, who were regarded as traitors by the Chinese, and the Luantung area swarmed with bandits, whose numbers had been swelled by desertions from the north-eastern troops. Moreover, the Japanese put their own interpretation on the withdrawal beyond the Wall, and still occupied Shanhaikuan and the passes, while the policing of the Peking-Mukden Railway was taken over by their garrison in Tientsin from Lutai to Shanhaikuan. Their troops at Kupeikou were supplied from Peking, and, to guard this line of communication, a garrison was maintained at Miyunhsien, only 40 miles from the old capital.
- 113. There was a further excuse for the maintenance of troops in this sector, for, during the first week in July, Feng Yu-hsiang seized the reins of government in Chahar from Sung Che-yuan, the chairman of the Provincial Government appointed by Nanking, and declared himself the head of an Anti-Japanese Salvation Army. This consisted of some of his old troops, under Fang Chen-wu and Chi Hung-chang, and all the undesirable elements which the Japanese had swept out of Jehol on their first advance.
- 114. Feng's patriotic attitude placed the Nanking Government in a dilemma. If they suppressed him by force they would arouse the resentment of Canton and brand themselves as friendly to the Japanese. If they left him alone, there was the risk that he might consolidate his position and become a threat to Peking. They accordingly massed a certain number of trusty divisions in the Hsuan Hua area, and attempted to negotiate for his retirement. This was accelerated by a threat on the part of the Japanese to drive him out and occupy Kalgan, and Feng retired to Taishan on the 8th August.
- 115. Sung Che-yuan returned to Chahar as chairman, and attempted to reorganise the troops, and reduced their numbers to a total commensurate with the resources of the province. Sun Tien-ying, who took no part in Feng's movement, was already at Paotouchen, nominally en route for the Tibetan border. Three or four leaders handed over their men or accepted posts under the chairman, but Fang Chen-wu and Chi Hung-chang, with about 6,000 ill-armed followers, remained recalcitrant, and an attempt to suppress them by force resulted in their crossing the border of Hopei at Tushihkou on the 16th September. Marching rapidly southward, they occupied Huaijou, only 30 miles from Peking. The town was also but 6 miles from Miyun, and altogether too close to the small Japanese garrison. The Kuantung Army accordingly served the rebels with a notice to leave the neutral zone in four days' time, stating that if they were not across the border by then they would take action against them. The Government troops round Peking were insufficient to deal with a sudden incursion of this nature, but by the expiration of the ultimatum four divisions were in position on the edge of the demilitarised zone. The Japanese sent a force in lorries to prevent the rebels breaking east to join the bandits in Luantung, and harassed them with bombers from the air. After testing the Chinese defences in several places, the rebels retreated to the hills, where, finding it impossible to subsist, they made a final effort to break through a fortnight later. Thoroughly dispirited by being harried from pillar to post, they surrendered and were disarmed at Shunyih, their leaders being given a safe-conduct for Tientsin on the 16th October.

Civil Wars.

Szechuan.

- 116. The civil war between Liu Hsiang and Liu Wen-hui, which ended in the favour of the former, during the autumn of 1932, was renewed in May by an attempt on the part of Liu Wen-hui to recover some of his lost territory. It is immediate adversary was Teng Hsi-hou, whose ally, Tien Tsung-yao, was then engaged in repelling a Communist incursion in the North. His first step was to insinuate his influence into Chengtu, where he hoped to gain control of the arsenal, so as to re-equip his troops. It had, however, been almost completely dismantled by Tien Tsung-yao, but he was able to transfer some of the still usable material to a workshop in the southern part of the city. Early in May a clash occurred between his troops and those of Teng Hsi-hou for a more complete control of the provincial capital and the rich districts of Central Szechuan. Tien Tsung-yao came to his ally's assistance, giving the Communists in the North a respite, of which they gladly availed themselves.
- 117. With the assistance of Liu Hsiang's XXIst Army, Liu Wen-hui was gradually driven out of Chienchow, Tenshou and Chengtu to the west side of the Min River to a narrow area bounded on all sides by hostile or barren territory.

Anti-Communist Campaigns.

- 118. The main preoccupation of the Central Government has been the attempt to suppress communism, and all their military effort has been directed towards the reclamation of the Province of Kiangsi. As far as financial assistance was concerned, the North was left to its own resources during the Japanese invasion of Jehol, and only sufficient troops were detached to maintain the loyalty of Hopei to the Nanking authorities. The whole year has been spent in preparations for a drive on an unprecedented scale with the object of eliminating all Red influence from Kiangsi. This is easier said than done, as the Communists are so firmly entrenched in the province that the slightest relaxation on the part of their opponents is a sure precursor of disaster. The driving force is supplied by the generalissimo himself, and his presence at the front is essential for the prosecution of his plans. His short absence in the North at the height of the Japanese invasion was the signal for an onslaught on two mobile columns of Government troops which were practically destroyed at Lo An. The Communists are desperate men, fighting in a friendly country on interior lines and under rigid discipline. Regularly paid, in their own currency, which the inhabitants are forced to recognise, they can supply most of their wants, in spite of the Government blockade, while the lack of certain commodities is an incentive to raiding. The country which forms their stronghold is excessively difficult and lacking in communications, and to attempt penetration without adequate roads is to invite disaster. Preparations for the encirclement and final annihilation of the Reds need time and money, neither of which can be afforded. Troops long in close contact are liable to succumb to Red propaganda, while the National Government is at its wit's end to finance the demands of the army Without pay the troops simply desert and sell their arms and equipment.
- 119. Their central position also confers an advantage on the Reds. The main weight of Chiang Kai-shek's attack is forty-five divisions on the line Yungfeng to Nanfeng driving south. To the south are the Cantonese forces, who may or may not be heartily in co-operation with the generalissimo's plan, and in Fukien is the XIXth Route Army, some Government divisions and the provincial levies. It is always open to the Communists to mass their whole force and strike at the weakest part of the circle. In July they broke into Fukien, outflanked the 78th Division of the XIXth Route Army at Liencheng and threw it on the defensive. On the arrival of reinforcements they withdrew with their booty, and at the end of August turned their attention to the northern part of the province, where they succeeded in capturing the City of Yenping after driving off the 56th Division and provincial levies. This town is only 90 miles from Foochow, and considerable nervousness was felt for the fate of the capital. The situation was, however, re-established by the arrival of the 61st Division from the lower Min River, and the Communists again withdrew, having replenished their supplies and munitions.

Szechuan.

- 120. The north-eastern part of the province has been organised as a Soviet State, and the leaders have taken advantage of all internal quarrels between the Chinese militants to extend their gains by raiding southward. The outbreak of hostilities between Liu Wen-hui and Teng Hsi-hou in early May was the signal for the irruption of the Reds from the Shensi border, who captured Nanchang. Tungchiang and Yaichow, from which they had been ejected after a previous raid early in the spring. Their occupation, however, was not of sufficient duration to establish a Soviet régime.
- 121. At the end of October the Communists made a much more serious drive, capturing Suanhan and Suitingfu, where they became a distinct menace to Wanhsien. Very serious losses were incurred by the Government troops opposing them, mainly owing to revolt on the part of Liu Tsun-hou's men. The general belief was that the IXth Communist Army would attempt to cross the Yangtze and effect a junction with Ho Lung.
- 122. The Government authorities were forced to denude the Chungking district of all available troops and take them down river to Wanhsien to cope with this menace.
- 123. On the 21st November Sanhwei was reoccupied and General Yang Sen recaptured Yingshan. Five armies were engaged in attacking the Communists from east, south and west, but had made little appreciable progress up to the 6th December.

Fukien Revolt.

124. On the 19th November Fukien declared independence, and the XIXth Route Army, which for some time had been extremely languid in the prosecution of the anti-Communist campaign, joined the movement against Chiang Kai-shek. Efforts at effecting a political settlement having failed, the Nanking Government began massing troops in Chekiang with a view to launching a punitive expedition from the North. A blockade of the ports was also declared, and the navy was ordered to co-operate in case landing operations were contemplated. The 56th Division stationed in the Kienning area remained loyal, and, in spite of threats to its communications from Fukien, advanced troops succeeded in holding out until a junction was effected with the 98th and 88th Divisions and some of the Salt troops. Chiang Kai-shek assumed personal command towards the end of December, and inaugurated a forward movement with Yenping as its objective. The main forces of the XIXth Route Army are in this area, but advanced elements, allegedly supported by Communists, have been threatening the invasion of Chekiang from the direction of Pucheng and Showning. Air raids by the Government forces have produced a good deal of moral effect, but the bombing of an independence meeting at Changchow has caused serious misgivings in the minds of the general public.

II.—FOREIGN RELATIONS.

(1) British Empire.

(a) United Kingdom.

of the year had, as is also described in the section on the League of Nations, most unfortunate reactions on relations between the United Kingdom and China. The misunderstanding which had arisen owing to the inadequate reporting of the Secretary of State's speech on the Lytton report at Geneva in December 1932 was still latent, and the continued failure of the League to give China satisfaction was attributed in the Chinese press to the machinations of His Majesty's Government in the United Kingdom. By the end of January a violent anti-British press campaign was, in fact, in full swing. His Majesty's Government in the United Kingdom were accused of abetting the aggressive designs of Japan as the result of some secret understanding with the Japanese Government, and credence was given to an alleged secret understanding between His Majesty's Government and the Japanese Government, under which, in return for our

support in the League discussions, Japan would give us a free hand in Tibet. At the beginning of February Reuter, on the authority of the Foreign Office, published official denials of these rumours, and confirmed the intention of His Majesty's Government to adhere to the Lytton report as the basis of their policy in the Sino-Japanese dispute. The publication of these denials marked the turning-point in the tide of the agitation, especially as they coincided with the Trival in Nanking of His Majesty's Minister, who had just returned from leave. Sir Miles Lampson's personal explanations of the policy of His Majesty's Government, combined with his strong representations against the continuance of this campaign, quickly brought it to a close, and by the end of February it had completely died down.

- 126. Relations between the United Kingdom and China since that date have remained undisturbed and have been particularly cordial during the latter part of the year. With the exception of the question of the kerosene oil regulations, reported in a separate section, and that of the strike at Butterfield and Swire's wharves at Canton, described below, neither of which were the concern of the Central Government, and both of which have been settled, there have been no new questions of importance which have arisen, while several old cases have been satisfactorily disposed of.
- 127. His Majesty's Minister left China at the beginning of December to take up his appointment as High Commissioner at Cairo. He is to be succeeded by the Hon. Alec Cadogan, C.B., C.M.G., who is expected to arrive early next year. Major-General O. C. Borrett, C.B., C.M.G., C.B.E., D.S.O., replaced Major-General J. W. Sandilands, C.B., C.M.G., D.S.O., at the beginning of the year as General Officer Commanding at Hong Kong, and Admiral Sir Frederick C. Dreyer, K.C.B., C.B.E., took over in March from Admiral Sir Howard Kelly, K.C.B., C.M.G., M.V.O., the command of His Majesty's ships and naval establishments on the China Station. Rear-Admiral F. G. G. Chilton, D.S.O., has succeeded Rear-Admiral R. A. S. Hill, C.B., C.B.E., as Rear-Admiral and Senior Naval Officer, Yangtze.
- 128. Wing-Commander R. P. Willock, Royal Air Force, has been appointed air attaché to His Majesty's Legation. He is the first British air attaché to this country. His headquarters will be in Shanghai.
- 129. Captain H. T. Baillie Grohman, D.S.O., O.B.E., left China in April for England, on completion of his appointment as head of the British Naval Mission to China. It is believed that the appointment will be allowed tacitly to drop, as the Chinese Government have not yet asked for a successor to be sent out, and Admiral Chen has explained that he is unable to do so at the moment owing to shortage of funds. The Admiralty have now decided that no further Chinese officers can be accepted for training, and Admiral Chen was so informed in reply to his enquiry whether four additional Chinese cadets could be sent for training to England. Captain Kelly's contract as naval instructor at the Chinese Mamoi Naval Academy at Pagoda anchorage has been renewed, and Instructor Lieutenant-Commander Taylor has replaced there Captain Munroe, who has returned to England owing to ill-health.
- 130. The Chinese Legation in London enquired last May of the Foreign Office their views as to the elevation of His Majesty's Legation to the status of an Embassy. Similar enquiries were made at Washington, Paris and Rome. After consultation with the other Governments concerned, His Majesty's Government in the United Kingdom replied that they did not consider the moment opportune for making any change.
- 131. Dr. T. V. Soong, then Minister for Finance, attended the World Economic Conference in London as chief Chinese delegate. During his visit he had conversations with the Secretary of State for Foreign Affairs, the President of the Board of Trade, and other prominent personages. Details of his visit are described in another section of this report.
- 132. His Majesty's Government in the United Kingdom, pending an opportunity of international consultation, imposed as from the 27th February, an embargo on the export of all arms and ammunition to either Japan or China. The embargo received unfavourable criticism from both sides. In this country

it was regarded as unfair to China, who was acting in self-defence and had to depend on foreign countries for supplies, while Japan was able to manufacture munitions of war herself. The embargo was removed on the 13th March, as there seemed no early prospect of international agreement on the subject, and it was felt that an embargo by Great Britain alone could not serve any useful purpose.

- 133. A delegation from Europe, headed by Lord Marley, to the World Anti-War Conference attempted in the autumn to hold the conference in Shanghai. Permission, however, was refused by the authorities of the International Settlement, the French concession and the Greater Shanghai Municipality. Attempts to hold the conference elsewhere in China were also unsuccessful but a private meeting, presided over by Lord Marley, was held at Shanghai on the 30th September, and was attended by some sixty delegates, claiming to represent various parts of China.
- 134. The case of the Anglo-Chinese College at Swatow, which has been turned into a municipal school, still remains unsettled, although it is hoped that recently some progress has been made.
- 135. An agreement was signed on the 8th November between the Asiatic Petroleum Company and the Haiteng District Government in respect of the company's installation at Sungsu. This question had been outstanding since 1928, when the company were compelled to leave their former installation at Amoy. An agreement with the local authorities had been reached in 1929, and the company had started work on their new site, but a year later the agreement was denounced owing to certain irregularities in its ratification, and it was only in November of this year that a final settlement was at last reached.
- An the 5th April the Eastern Extension, the Great Northern and Commercial Pacific companies signed new agreements with the Ministry of Communications. The former agreements and landing licences of the cable companies, including those of the Japanese Telegraph Administration, had expired on the 31st December, 1930. Draft agreements drawn up by the companies were, with the exception of that of the Japanese company, finally officially approved by the Chinese Government at the end of December 1931. The other three companies, ascertaining the position with regard to the Japanese agreement, wished to make certain modifications in their agreements, so as not to be placed at a disadvantage with the Japanese company. Negotiations proceeded without success all through 1932, and in the middle of February 1933 the companies were given a week's notice to conclude the agreements as approved. The Eastern Extension Company thereupon invoked the assistance of this Legation, who had not previously been kept informed as to the position of the negotiations. As a result of repeated unofficial representations, and after much discussion, the agreements were finally signed in their original form, while the companies received a written assurance from the Ministry of Communications that they would not be subjected to any unfair competition through their having signed the agreements.
- 137. On the 16th April the Chinese customs prevention launch *Chenan* was pirated and looted in Lappa district. Two British officers—Pearce, who was in command, and Baldwin—were killed, and also a Chinese engineer.
- 138. In China proper there have otherwise been no cases this year of kidnapping or banditry involving British subjects. There is, however, reason to regard as confirmed the reports of the deaths of the Rev. H. S. Ferguson and Mr. Edwards (see annual report 1932, paragraphs 52 and 53).
- 139. At the end of 1932 a note was received from the Waichiaopu requesting that instructions should be issued to British subjects to pay frontage fees and take out licences in compliance with the revised regulations governing the use of water frontage at Shanghai. At the beginning of January all foreign firms in Shanghai owning riparian properties received a request from the Chinese Land Bureau to pay water frontage licence fees. His Majesty's Minister pointed out to the Minister for Foreign Affairs in February the undesirability of the Chinese pressing the question which had remained dormant for two years, and a strong attitude was taken up by the Americans and Japanese, who maintained

that the enforcement of these regulations would be a violation of existing treaty rights. In consequence probably of these representations, the question has been allowed to drop.

- 140. The attempts made by Messrs. Butterfield and Swire to reform the vicious "tea boy" system in the Yangtze was the cause of a serious agitation against the company by the Canton Seamen's Union, who were not directly concerned in the question. The "tea boy" system in question dates from the time when steamers first ran on the river. The "tea boys," who act in the capacity of stewards for the Chinese passengers, are unpaid and get a living from what they can extort from the passengers. This system led to such abuses that the company decided at the end of last year that an attempt should be made to abolish it. Accordingly, as an experiment, the "tea boys" on one of the ships, steamship Woosung, were dismissed and replaced by paid stewards. Minor incidents occurred at Shanghai and Hankow after the dismissal of the "tea boys," but no serious trouble was experienced until the Canton Seamen's Union, who are stronger than that at Shanghai, took up the question. An abortive conference took place between the union and the company, and in the middle of June the union compelled the employees at Butterfield and Swire's wharves at Canton to come out on strike. The situation was complicated by the political motives which were behind the agitation, and it was not until the end of November that a settlement was at last reached and the strike called off.
- 141. The position with regard to the unauthorised searching of British vessels for opium, arms, &c., by Chinese armed police and soldiery has improved very considerably. His Majesty's Minister, on his return from leave at the beginning of the year, took this question up strongly with the Ministry for Foreign Affairs, and stated that, if further incidents occurred, he would be forced to arrange for armed guards to be placed on the British vessels concerned. There has since been only one case of an unauthorised search, and as this occurred a short time after His Majesty's Minister's representations, it may, perhaps, be assumed that the Waichiaopu had not by then caused the necessary instructions to be issued. While last year there were frequent complaints of irregular searching of ships at Shanghai, this year none have been received. The Kiangsi Narcotics Bureau, which was chiefly responsible for the searches on the lower river (Nanking to Shanghai), where most of the incidents took place, has now been reorganised, so as to be directly under the control of the Central Government.
- 142. The question of the carrying of Chinese troops on British ships arose this autumn during the Communist scare at Wanhsien (see also section on Communism). The local authorities stated that, unless troops could be despatched at once down the river, Wanhsien would fall into the hands of the "Reds." His Majesty's Minister informed the shipping companies that the decision must, of course, rest with them, but his own view was that it would constitute a dangerous precedent, and he was not prepared to advise them to depart from their previous attitude of refusing to carry Chinese troops. Nevertheless, the companies decided to transport a certain number of Chinese troops accompanied by naval guards from the British gunboats.
- 143. A note was received from the Waichiaopu in July requesting His Majesty's Minister to make urgent representations to the Hong Kong Government to abandon the scheme for the construction of a public park in Kowloon City, involving the evacuation of Chinese residents, and contending that the proposed action was a violation of former agreements. The matter is being investigated by the Hong Kong Government, who state that, in any case, the removal of inhabitants will not be required until the end of 1934.
- 144. The question of the position of Chinese consular officers in Malaya, which had been causing some trouble to the Malay Government, was settled at the end of August by an exchange of letters between the Minister for Foreign Affairs and Mr. Ingram (on His Majesty's Minister's behalf). It was thereby agreed that Chinese consular officers in Malaya would be under the general supervision of the Chinese consul-general at Singapore, through whom all correspondence with the Governor would in future be conducted.
- 145. As it was considered that with the establishment of Iraq as an independent State any attempt to claim British jurisdiction for Iraqi nationals

would almost certainly be challenged by the Chinese authorities, it has been ruled that Iraqis shall no longer be registered as British-protected persons, and that they shall be regarded as having ceased to possess extra-territorial rights. They will, however, continue to receive British diplomatic protection and the good offices of His Majesty's consular officers when the circumstances warrant it.

146. The Waichiaopu have at last replied to our memorandum of the 11th February, 1930, in which the proposal was made that British subjects of Chinese race when paying transient visits to China should be registered in His Majesty's consulates and receive British protection. The Chinese Government, while recognising the dual nationality of persons born of Chinese parents in British territory, refused to admit that such persons can be divested of their Chinese nationality. The Vice-Minister for Foreign Affairs gave, however, His Majesty's Minister a verbal assurance that there would be no difficulty in regard to the issue of denationalisation certificates provided the requirements of the law were met.

(b) Canada.

- 147. On the 2nd February His Majesty's Legation notified the Chinese Government that Mr. Paul Sykes, who had previously been Canadian Trade Commissioner at Dairen, had moved his headquarters to Tientsin, and that his district would now include the whole of North China.
- 148. The Canadian Trade Commissioner at Shanghai approached His Majesty's commercial counsellor in June with a request that a protest should be made to the Chinese Government against the new import duties on flour and dry salt, herring and salmon. The question was referred to the Foreign Office, who replied that Colonel Cosgrave should be informed that the items in question would be included within the scope of any discussions which might be initiated in the matter with the Chinese authorities.
- 149. Some difficulty has been experienced both at Canton and Shanghai owing to the action of the local anti-Japanese boycott associations in interfering with the importation and distribution of consignments of Canadian salt herrings. At the beginning of 1933 His Majesty's consul-general at Canton furnished all possible assistance to the Canadian Trade Commissioner at Hong Kong, and a working arrangement was eventually evolved with the Chinese authorities to facilitate the proper handling of any future shipments. At Shanghai representations were made in February to the mayor by His Majesty's consul-general at the request of Colonel Cosgrave for the release of similar consignments by the Anti-Japanese Boycott Association at Kiangyin. As a result of this action, the matter was satisfactorily settled and no further trouble has been reported.

(2) Japan.

- 150. The history of Sino-Japanese relations in North China, which comprises the capture of Shanhaikuan on the 1st January, the fall of Jehol several weeks later, the events leading up to the advance of Japanese troops early in May to within a short distance of Peking, and, finally, the signature of the Tangku armistice on the 31st May and the execution of its provisions, is very closely connected with Chinese internal politics and is dealt with in its different aspects in those sections on military operations, the internal political situation, and Manchuria. Reference is also made to Sino-Japanese relations in the section on the League of Nations.
- 151. Several incidents have occurred which have threatened to increase the already existing tension in Sino-Japanese relations. In May a Japanese sentry standing outside the Japanese Legation in Peking was assaulted and wounded by an unknown Chinese. The aggressor was arrested by Japanese troops, and is, as far as is known, still incarcerated in the Japanese Legation Guard compound. The incident, which was followed up by the reinforcement of the Legation Guard from Tientsin, formed the subject of discussion between the interested heads of missions, but no action was taken. A further incident took place in Peking on the 21st June, when Chinese soldiers, in the course of a quarrel, discharged their revolvers in the close proximity of Japanese troops.

Both incidents were taken up by the Japanese authorities, but lead to no complications. On the 15th October the Japanese authorities arrested a Korean in a suburb of Canton without previously notifying the Chinese police, and brought the prisoner to the Japanese consulate in the French concession. The local authorities were indignant at this action, but the matter seems to have been allowed to drop.

- 152. Mr. Yoshizawa visited China at the end of March with the alleged intention of getting into touch with the Chinese Government for the purpose of negotiations. The Minister for Foreign Affairs informed Mr. Ingram on the 30th March that the Chinese Government would exercise the utmost caution in their dealings with him. In conversation with His Majesty's Minister in Peking in April, Mr. Yoshizawa agreed that for the time being there was no possibility of any compromise discussions with China over the Manchurian issue. His mission apparently met with but little success.
- 153. Dr. Sugimura's visit to China in October, in view of his former connexion with the League of Nations, was looked upon as an indication of the desire of the Japanese Government to proffer Japanese technical assistance to Chinese political leaders, as a set-off to that recently secured by Dr. T. V. Soong through the League of Nations.
- 154. The new Japanese barracks at Shanghai was completed by the end of September and have now been occupied by the Japanese main contingent. It is understood that there is accommodation for 3,000 to 3,500 men. The construction of the barracks, particularly in view of its strength and permanence, has aroused certain apprehension in the Chinese press and in other circles.
- 155. Developments in the extra-settlement road question are dealt with under a separate section of this report. Suffice it to say that the attitude of the Japanese authorities still constitutes the chief stumbling block in the way of the conclusion of any agreement.
- 156. Anti-Japanese boycott associations still continue their activities unabated, the strength of which varies according to the political atmosphere of the moment and the measure of control of the local authorities in the particular districts in which they are being directed. In Shanghai, as a result of effective police action, the bombing activities of the so-called patriotic groups aimed at shops dealing in Japanese goods have appreciably diminished. Recorded imports of Japanese goods are being maintained at about half the pre-boycott figures. It may be said that the anti-Japanese boycott situation in Shanghai has progressively become easier in view of the absence of real patriotic feeling behind the movement. The chief manifestations of the movement now lie in the opportunities it affords to racketeering organisations to exploit it for the purpose of enriching themselves by terrorist methods. In Canton, on the other hand, the intense interest focussed on the Sino-Japanese crisis has resulted in the frequent seizures of Japanese goods, and numerous cases have occurred when people have been fined or executed for dealing in prohibited goods. At Hankow it is reported that the tightening of the boycott has brought Japanese trade to a standstill.

(3) Russia.

157. M. Bogomoloff, the newly-appointed Soviet Ambassador, arrived in China on the 23rd April, and proceeded a few days later to Nanking to present his credentials. On his arrival in Peking M. Bogomoloff raised the question of the evacuation of the Russian Guard compound by the detachment of United States marines, who had taken over that portion of the defence of the Legation quarter after the Chinese raid on the premises in 1927. A meeting of the interested Ministers was convened, at which it was agreed to withdraw the United States detachment forthwith.

158. Since the resumption of relations between China and the Union of Soviet Socialist Republics at the end of 1932, there has been little progress in the Sino-Soviet negotiations for a pact of non-aggression, although the matter still continues to be under consideration by the Chinese Government. During the summer the latter submitted a draft text of such a pact to the Soviet Government, which contained numerous provisions which were considered impossible of

acceptance, such as a mutual engagement not to recognise Manchukuo. The Soviet Ambassador handed a counter draft to the Chinese Government in October eliminating the objectionable provisions, the draft being based on the Soviet non-aggression pacts with the Baltic States.

- 159. In June the Soviet consul-general at Shanghai called on the senior consul with the request that he should take part in consular body meetings. It was decided that the Soviet consul-general should be treated in the same way as the German consul-general (see section on Germany).
- 160. The question of Sino-Soviet relations is also referred to in the sections on Manchuria, Communism and Sinkiang.

(4) United States of America.

- 161. Throughout the year close co-operation has existed between His Majesty's Legation and the United States Legation in the matter of consultation and representations to the Chinese Government on all matters affecting the interests of the two nations.
- 162. The capture of Shanhaikuan by the Japanese in January and the possibility of further developments in North China raised the question of the desirability of mediation between the Chinese and Japanese. The United States Minister informed His Majesty's Chargé d'Affaires that the State Department regarded any efforts at conciliation as unlikely to succeed unless the initial move came from the Chinese and Japanese and that, although ready to consider sympathetically any proposals, it would not take the initiative itself. When the Chinese Government, in their note of the 10th January, called the attention of the interested Governments to the fact that the Japanese had taken advantage of the special privileges under the 1901 protocol, the United States Minister, at a meeting of colleagues on the 17th January, stated that the view of the State Department was that, if the Chinese Government pressed for a reply, they should be informed orally that the note was looked upon as a Chinese declaration for purposes of record, requiring no reply. He added that the State Department had informed the Chinese Legation orally that it believed that the circumstances of the Japanese occupation of Shanhaikuan flowed from factors arising out of the conflict between China and Japan and not from provisions of the Boxer protocol.
- 163. At the meeting of the Advisory Committee on the Sino-Japanese dispute at Geneva on the 17th March, communication was received from United States Government appointing a delegate to participate in the work of that body without the right to vote.
- 164. In April Dr. Nielsen, an American medical missionary, was captured by bandits at Hsiuyen. After fruitless attempts to secure his release, he was finally liberated in November. It is believed that his release was effected on payment of 10,000 dollars by the mission authorities.
- 165. Rumours to the effect that the State Department was seriously considering the transfer of the United States Legation to Nanking was emphatically denied by United States Minister in July.
- 166. Reports had appeared in the press in May that Chinese representatives of various Ministers had been delegated to serve on a Sino-American committee to deal with public and private debts due to Americans. The United States Minister informed His Majesty's Minister confidentially in July that he was, in fact, engaged in discussions with the Waichiaopu regarding the establishment of such a committee for the consideration and assessment of claims.
- 167. The question of the 50 million dollar loan to China to facilitate the purchase by the Chinese Government of cotton and wheat is dealt with in the Finance Section of this report.
- 168. In December the Chinese Government exercised their right to demand a revision of the Treaty for the Extension of the Commercial Relations between the United States and China. Article 17 of this treaty lays down that either of the high contracting parties may demand a revision at the end of successive periods of ten years from the date of the exchange of ratifications, *i.e.*, the 13th

January, 1904; but that if no revision is demanded before the end of a decennial period the treaty shall remain in full force for a further term of ten years. The United States Minister has, it is understood, simply referred the Chinese Government's demand to the State Department.

(5) France.

- 169. In July considerable publicity was given in the press to the occupation by certain units of the French navy of various coral reefs situated between French Indo-China and the Philippine Islands. The question was investigated by the Chinese authorities at Nanking and Canton, and informal enquiries were made of the French Legation as regards the position of the islands. In conversation with His Majesty's Minister, the French Minister stated that the reefs were of little use and that the Japanese Government had also been making representations on the subject at Paris. Agitation in China over the annexation quickly died down.
- 170. Negotiations between the French Legation and the Chinese Government with a view to reaching agreement as to the modifications to be introduced into the Treaty of 1930 between China and Indo-China have been proceeding during the year, and reached a point in the late autumn when signature was imminent. This precise moment was chosen by Canton to impose an additional tax on the import of rice. The Government of Indo-China, which was hard hit by this move, took prompt umbrage, and the French Minister was instructed not to sign the agreement.
- 171. When in Europe for the London World Economic Conference T. V. Soong paid two short visits to France in July, and was awarded the highest rank of the Legion of Honour by the French Government.
- 172. Some interest was aroused in August by the arrival in Manchukuo of M. D'Ollivier, representing the National Association of Economic Expansion, with a view, it is understood, to exploring the possibility of the investment of French capital in connexion with the development of that country. It has not been found possible to ascertain exactly what progress, if any, has been made by M. D'Ollivier in his task, but according to a report published by the Manchukuo News Service he stated that negotiations with the South Manchuria Railway for joint Franco-Japanese capital investment in Manchukuo had been satisfactorily concluded at Dairen on the 13th October, and that he was carrying on further conversations with the Kuantung army, the Japanese Embassy and the Manchukuo authorities, and that he expected to sign an agreement shortly with the vice-president of the South Manchuria Railway.

(6) Germany.

- 173. General von Seeckt paid a visit to China during the summer. Although it was thought that he had come to review and submit recommendations to the Chinese military authorities, Lieutenant-Colonel Heinz, of the German Military Mission, who accompanied him to Peking, assured the military attaché to His Majesty's Legation that the general was touring the Far East for reasons of health.
- 174. In March the German Minister, in conversation with His Majesty's Minister, raised the question of the position of the German consul-general at Shanghai as regards participation in meetings of the consular body when such matters as the Land Regulations were discussed. The practice at Shanghai had been that the German consul-general attended all ordinary consular body meetings, but not those at which questions involving the Land Regulations or extra-territoriality were discussed. Dr. Trautmann has not reverted to the matter.
- 175. During the summer Dr. Jänicke, former Regierungspräsident of Potsdam, arrived in Nanking as one of the two expert advisers on the reform of the Chinese Civil Administration. In July His Majesty's Embassy at Berlin reported that Dr. Nign, representative of the Association of Chinese

Industrialists, arrived in Berlin for the purpose of gathering information on the National Socialist movement and the German industrial, commercial and banking organisations.

- 176. The Nazi propaganda film "Deutschland Erwacht" has been shown at various centres in China, but does not seem to have evoked very great enthusiasm except among the Nazi members of the audiences before whom it was exhibited.
 - 177. Dr. T. V. Soong also visited Germany during his trip to Europe.

(7) Italy.

- 178. Italian activities have chiefly been centred on the development of aviation and the sale of Italian machines and material (see section on Aviation). Dr. T. V. Soong paid a visit to Italy in July, in the course of which it is understood that arrangements were made for the employment of Italian aviation personnel and material in China. He was awarded a high Italian decoration.
- 179. After the conquest of Jehol by the Japanese in March, Marshal Chang Hsueh-liang left Peking for Shanghai, and proceeded to Italy in the following month, where he took up his residence for several months.
- 180. Count Ciano de Cortallezzo, who was appointed Italian Minister to Peking in October 1932, left Shanghai for Italy in April, and has, it is understood, been appointed chief of the Press Bureau at the Palazzo Chigi. He has been succeeded by Commendatore Boscarelli, formerly Italian Minister to Cuba, who arrived in China at the end of November. Like his predecessor, the new Minister intends to reside chiefly at Shanghai.

(8) Netherlands.

181. During the early part of the year the Netherlands Legation were chiefly occupied with their negotiations, completed in April, with the Chinese Government concerning the remission of their share of the Boxer indemnity (see section on Boxer Indemnity). In addition, they have been following carefully the affairs of the Chefoo Harbour Improvement Commission on account of the interest which the Netherlands Harbour Works Company has in the proposed scheme for the provision of additional berthing facilities at Chefoo (see section on Customs and Tariffs).

(9) Belgium.

- 182. The Belgian Legation has during the year been largely occupied in trying to obtain payment of arrears to the bondholders of the Lunghai Railway, one of the chief Belgian interests in China, and protect them from a diversion of the railway's earnings for the purpose of extending its operations (see section on Railways).
- 183. Early in August T. V. Soong paid a visit to Belgium and received the Grand Cordon de l'Ordre de la Couronne.

(10) Treaties.

- (a) Treaties with Secondary Powers.
- 184. As far as is known, no progress has been made with regard to the proposed treaty of amity and commerce between China and Siam. His Majesty's Minister at Bangkok reported at the end of 1932 that the Siamese Minister for Foreign Affairs had met Mr. H. S. Chu, of the Chinese Ministry for Foreign Affairs, and that the latter had raised the question of treaty negotiations.
- 185. His Majesty's representative at Panamá was informed in January by the Panamanian Minister for Foreign Affairs that the Chinese Chargé d'Affaires had been pressing for the conclusion of a treaty of amity, commerce and navigation. The matter is apparently still under consideration.

186. At the end of October a Kuomin News Agency report appeared to the effect that the Chinese Ministry for Foreign Affairs were contemplating the conclusion of a treaty of commerce and amity with Spain. Enquiries at the Spanish Legation elicited the fact that conversations were taking place with a view to improving Spanish trade with China.

(b) Tabular Statement.

187. (1) Treaties, &c., negotiated and entering into Force in 1933.

With-	Place and Date of Signature.	Subject.	Place and Date of Exchange or Deposit of Ratifications.	Date of Entry into Force.	Remarks.
United Kingdom, Brazil, France, Netherlands, Norway and United States of America	Exchange of notes, Nanking, Feb. 8-12, 1933	Chinese courts in the International Settlement at Shanghai	Nanking, Feb. 8-12, 1933	Apr. 1, 1933	Renewal for period of three years of agreement and exchange of notes of Feb. 17, 1930.
Netherlands	Exchange of notes, Apr .4, 1933	Remission as from Jan. 1, 1926, of all payments due from Chinese Government on	Nanking, Apr. 4, 1933	Apr. 4, 1933	
United King-	Exchange of letters, Nanking, Aug. 8, 1933	account of the Boxer indemnity Position of Chinese consular officers in Malaya	somethic in a enoise was for all orang multarissome	Aug. 8, 1933	and an era present

(2) Treaties, &c., denounced in 1933.

Japan	notes, Nan-	Sino-Japanese Tariff Pact valid for three years	Nanking, Ma 6, 1930	May 6, 1930	Expired 1933.	May	6,
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(11) League of Nations.

188. The question of a conciliatory solution of the Sino-Japanese dispute in connexion with Manchuria was still engaging the attention and activities of the League of Nations at the beginning of the year. At the end of 1932 the Committee of Nineteen adjourned till the 16th January, leaving the President and Secretary-General to continue discussions with the parties concerned on the basis of the draft resolution and statement of reasons of the 15th December, 1932. The committee met on the 16th January, and, after exploring every avenue of approach, found itself obliged to report, on the 21st January, to the Assembly that, in view of the decision of the Japanese Government not to accept the draft resolution of the 15th December, even if the impossibility of inviting non-members to take part in the negotiations were eliminated from the draft, and of the amendments desired by the Chinese side, its attempts to propose a procedure for settling the dispute had failed. The committee, however, decided to begin forthwith the preparation of its draft report, under paragraph 4 of article 15 of the Covenant.

189. On the 1st February the Drafting Committee of Nine appointed to prepare the report completed the first three parts dealing with the historical background and the action taken and conclusions reached at Geneva. The final portion, making recommendations, which closely followed those contained in the Lytton report, was completed shortly afterwards. Attempts were made at this stage by the Japanese delegates to meet the views of the Committee of Nineteen as regards conciliation, but the proposals were not considered to

constitute a satisfactory basis. The report was finally approved by the Committee of Nineteen on the 13th and 14th February, and referred to the Assembly for adoption. The latter approved it on the 24th February by 42 votes to 1, Japan alone voting against, and Siam abstaining. The Japanese delegate then announced that Japan could no longer co-operate with the League in their difficulties with China whilst the Chinese representative accepted without reserve the recommendations of the report. On the same day, particularly in view of the threatening situation in Jehol, an advisory committee of twenty-one was set up to follow the situation in China. This committee was also requested to assist members of the League in concerting their action and their attitude among themselves and with the non-member States so as to conform with their decision not to recognise the existing régime in Manchukuo. The committee accordingly drew up certain technical recommendations, which were transmitted to members of the League on the 14th June, and were accepted by His Majesty's Government in the United Kingdom. As regards the postal services, which was, perhaps, the most actual question dealt with, the committee thought it sufficient to remind members of the League that Manchukuo was not a member of the Universal Postal Union, and that, on the 24th July, 1932, the Chinese Government had requested the union to notify all member States that all postal services in Manchuria had been temporarily suspended, and that all stamps issued by the puppet Government would be invalid.

- 190. During this critical period the activities of the League were followed in China with particular attention. Any step or proposal which was thought to savour of pro-Japanese bias was immediately given full publicity and strenuously attacked in the press. The intentions of His Majesty's Government, in particular, were for a time the centre of bitter attack, and it was only after considerable effort that Chinese misapprehensions were completely allayed. In a press interview on the 19th January Dr. Lo Wen-kan expressed his disappointment over the weakness and procrastination of the Committee of Nineteen, and, in conversation with the United States consul-general at Nanking a few days later, he even suggested that, if China failed to obtain justice from the League of Nations, she might be compelled, owing to the revulsion of public opinion, to withdraw altogether from that body.
- 191. In view of the relaxation in the tension in Sino-Japanese relations, the desire of the Chinese Government to avail itself of the technical services of the League of Nations in its task of industrial reconstruction has much increased. In June the Chinese Government requested the Secretary-General of the League of Nations to place at its disposal the services, for one year, of a technical agent as a liaison agent for technical co-operation between the National Economics of China and the competent organs of the League of Nations. The question was considered at a special meeting of a League of Nations Council Committee, held in Paris in July, when Dr. Rajchman was selected as chief technical delegate to the Chinese Government.
- 192. Dr. Sugimura, former Under-Secretary-General of the League of Nations, arrived in Shanghai on the 17th October on a tour of inspection of the principal cities of China.

(12) International Settlement at Shanghai.

(a) Sino-Japanese Armistice Agreement.

193. The question of the interpretation of article 2 of the Sino-Japanese Armistice Agreement of the 5th May, 1932, arose again in February, when the Japanese raised objection to certain Chinese troops movements through the prohibited area en route from Nanking to Hangchow. Although the Chinese authorities repeated the verbal assurances previously given that such troop movements would be notified to the Japanese authorities as a matter of courtesy, but not of right, the Japanese consul-general at Shanghai was not satisfied. On instructions from His Majesty's Minister, His Majesty's consul-general at Shanghai informed his Japanese colleague that, if he pressed the point, it might lead to a reconsideration by the neutral Governments of the whole position of the Joint Commission, and that, in view of the fact that the Chinese authorities were evidently prepared to give verbal satisfaction, it appeared unwise to force what seemed an unnecessarily dangerous issue. On being apprised of His

Majesty's Minister's views, the Japanese colleague said that he had lodged a strong protest with the Chinese authorities about the transport of troops by railway through the prohibited area. Shortly afterwards, however, the Japanese Minister informed Sir J. Brenan that he hoped that it would be possible to arrange matters with the Chinese authorities without troubling the joint commission.

194. At the end of November, with the transfer of Central Government troops from the Yangtse area southwards to deal with the situation in Fukien, there has been a recrudescence of complaints by the Japanese of the movements of such troops through the demilitarised zone, but serious friction has so far been avoided by the obvious genuineness of the Chinese representatives' desire to comply with the Japanese requirement that preliminary notice of such movements be given to them. It is clear, however, that the Japanese are determined not to allow the agreement to fall into desuetude.

(b) Extra-Settlement Roads.

At the beginning of the year discussions were still proceeding between the Shanghai Municipal Council and the Japanese consul-general, and the Shanghai Municipal Council and the Chinese municipal authorities, with a view to reaching a solution of the extra-settlement road problem. The principal obstacle which had arisen concerned the insistence of the Japanese authorities in claiming a special position in the proposed police force for the outside roads areas and the Chinese refusal to recognise any such claim. At the end of 1932 the Japanese consul-general, in conversation with His Majesty's consul-general, appeared to be more accommodating, and proposed certain modifications in the draft agreement initialled by the representatives of the Shanghai City Council and the Shanghai Municipal Council in June 1932, the most important of which related to the posts in the police force to be allocated to Japan and the general employment of Japanese police in this force. The proposals were looked upon as more hopeful by Mr. Fessenden, secretary-general of the municipal council, who proposed to get them modified in a form more likely to be accepted by the Chinese. Further conversations took place between the Japanese consul-general and Mr. Fessenden in March, when the former stated that his Government insisted on a previous guarantee that the requirements regarding the appointments of senior Japanese police officers in the northern and western districts must be met before they would consent to the conclusion of any agreement. There the matter apparently rested, and in view of Chinese opposition to the Japanese requirements negotiations reached a deadlock.

196. In October His Majesty's Minister visited Shanghai and discussed the whole question with Mr. Bell, chairman of the municipal council. After considering the matter with his British and American colleagues on the council, Mr. Bell communicated to His Majesty's Minister a memorandum defining his views as to the time in which a settlement might be reached. A few days later His Majesty's Minister met the Japanese Minister, and after emphasising the unfortunate effects of the deadlock which had occurred left with him for his consideration a formula which might serve as a basis of agreement. At Nanking on the 10th October Mr. Ariyoshi handed to Sir Miles Lampson his counterproposals, which had not yet, however, received the approval of his Government. The acting British consul-general was instructed to discuss these counterproposals with Mr. Bell, and later reported that they had been accepted in principle by the British and American members of the municipal council. On the 21st October the Japanese consul-general informed the acting British consul-general that the counter-proposals had been approved in principle by the Japanese Government, and Mr. Davidson, with his United States consular representative, interviewed the mayor, on the 25th October, to suggest the resumption of negotiations at the point where they were left in the spring with the Japanese counter-proposals as a basis. The mayor referred to the Chinese Government for instructions, and Mr. Ingram at the same time pressed the Waichiaopu to expedite a settlement.

197. Mr. Ingram was, however, informed by the Vice-Minister for Foreign Affairs on the 21st November that, while the Chinese Government were most grateful for His Majesty's Minister's efforts to get this question settled, they

could not agree to the new proposals, which were admitted by an advance, as they considered that they would be difficult to work in practice, and would probably be misunderstood by the Chinese public in view of the existing state of relations with Japan and China. The mayor a few days later sent a similar message to Mr. Davidson. There the position remains at the end of the year, although the mayor has expressed his willingness to discuss certain minor issues, which have been causing some inconvenience. It would appear that the Chinese do not at present want a settlement of this question, but in the meantime there have occurred a number of small incidents in the western district which would tend to show that the Chinese have abandoned the tacit agreement to avoid provocative action.

(c) Chinese Courts in the Settlement.

198. At the beginning of the year His Majesty's Minister met in Shanghai the Joint Commission of the British Chamber of Commerce and China Association and the British members of the municipal council, and explained to them the lines which he proposed to follow for the extension of the Shanghai Court Agreement (as opposed to its revision) on its expiry on the 1st April. No opposition was raised, although emphasis was placed on the need for securing assurances from the Chinese Government for remedying the alleged defects in court procedure, which had formed the subject of recent agitation amongst the foreign community at Shanghai.

199. In February negotiations on the subject were opened with the Chinese Government, and after some discussion it was finally decided that the extension of the court agreement should be effected by two sets of exchange of notes, the first providing for the extension of the agreement for a further period of three years, and the second covering certain assurances in regard to reforms in civil proceedings, with special reference to matters of appeal and execution of judgment. In addition the interested foreign representatives arranged to renew their unilateral declaration of the 17th February, 1930. The notes having been duly approved by the Chinese Government and the foreign representatives concerned were signed on the 8th February.

200. In reply to enquiries by Mr. Ingram two months later as to what progress was being made in regard to the implementation of the assurances, the Waichiaopu stated that the matter was engaging the active attention of the Ministry of Justice, who were at present examining M. Padoux's preliminary recommendations. M. Padoux did, in fact, meet the consular representatives of the Powers concerned and other interested personalities at Shanghai on the 7th April informally, with a view to dealing with the criticisms on the foreign side levelled at the present judicial system. A further meeting was held on the 30th June, at which M. Padoux communicated copies of certain regulations relating to execution in civil cases and points of procedure to be observed which had been issued by the Ministry of Justice to the authorities concerned with a view to securing improvement on judicial procedure. It now remains to see whether the action taken by the Ministry of Justice will have satisfactory results.

(d) Factory Legislation.

201. Owing to the need in the interests of the Chinese factory workers in the Chinese and foreign-owned factories in the International Settlement of taking steps to ensure a proper measure of superintendence over the internal arrangements of the factories, the council of the International Settlement during the spring passed a new bye-law in spite of opposition on the part of the Chinese authorities, enabling them to take the requisite action in the matter. Negotiations then took place between the foreign and Chinese municipal council for some arrangement under which the former would enforce in the International Settlement a system of factory inspection uniform with that enforced by the Chinese authorities in the Chinese-controlled areas outside. The negotiations at the end of the summer had reached a deadlock on the point of control of the inspection of factories in the settlement. The council of the International Settlement were prepared to accept any compromise provided that the administrative control of the council of the settlement in this question remained unimpaired. His Majesty's Minister discussed this question with the Waichiaopu on his visit to

Nanking in October, and pressed the Chinese authorities to reach a solution of this question on the basis of the standpoint of the council, which appeared to him fair and reasonable. The Waichiaopu suggested that some formula for a joint arrangement might be evolved, such as the joint commission in the case of the Court Agreement of 1930. The acting British consul-general, Shanghai, was informed of the tenor of His Majesty's Minister's discussions on the subject that the Waichiaopu in the hope that he and the chairman of the municipal council might be able to write out some solution on the lines suggested. At the end of October the Waichiaopu defined their suggestion, which amounted to (a) the operation of the Factory Law in the settlement; (b) actual inspections to be carried out by Chinese Government and settlement inspectors in co-operation; and (c) establishment of a board composed of equal numbers of Chinese and settlement representatives to decide any points in dispute. No further progress was made with this question before the end of the year.

(e) Shanghai Municipal Council and the Chinese Telegraph Administration.

202. A controversy of, at the moment, secondary importance has arisen between the Shanghai Municipal Council and the Chinese Telegraph Administration. The dispute in question concerns the underground cables which link up the Post Office of the Chinese Telegraph Administration at Markham Road, which lies about 240 feet inside the settlement boundary, with the ordinary Chinese telegraph system outside the settlement. These cables are owned by the Chinese Telegraph Administration, who now wish to lay fresh cables to connect with the new Marconi wireless station at Chenju. The Shanghai Telephone Company is desirous of laying these cables for the administration and to rent them at a nominal cost, but the administration is insisting upon absolute ownership. The council bases its attitude on the fact that it has certain obligations arising out of the Telephone Franchise which it granted to the Shanghai Telephone Company in 1930. The Minister of Communications appealed in October, through Mr. Ingram, to His Majesty's Minister to help to effect a settlement of this question, but it is hoped that this will, nevertheless, be solved by direct negotiations with the Ministry of Communications and the municipal council.

III.—RAILWAYS.

General.

The situation in regard to the Chinese railways shows little improvement. In fact, it may well be described as one of the least promising features in the reform of government administration in this country, for, in contrast with the Ministry of Finance, where very considerable reorganisation has been effected under the able guidance of Dr. T. V. Soong, the Ministry of Railways remains an inefficient, not to say corrupt, department of the Government. The reasons are not altogether unconnected with internal politics, for it is known that the Ministry has for years past been a bait offered to the Cantonese faction to ensure their co-operation at Nanking, beginning with Mr. Sun Fo's incumbency of the post. They have treated it as a milch cow. The present Minister, Mr. Ku Meng-yu, is a semi-invalid and rather incompetent adherent of Mr. Wang Ching-wei, while the Vice-Minister, Mr. Tseng Chung-min, was admitted by the Minister of Finance to be nothing short of dishonest. The problem of the now immense and ever-increasing load of debt of the State railways is one that demands the utmost economy, efficiency and honesty of administration. Unfortunately it is one with which the Minister of Finance has steadily refused to associate himself. In fact, his plea that the Government has balanced its budget, while the railways continue to default for very large sums, has drawn forth bitter criticisms from the foreign bondholders, who have, in the case of certain railways, formed associations to assert their rights and press for more efficient administration.

204. Attention is drawn in greater detail below to the appropriations from various railways for military expenditure, and for the financing of new construction on other lines, at the expense of the bondholders and creditors of the railways from which such funds are drawn. Sometimes these appropriations are made quite openly; occasionally, less honest practices are resorted to, and sums owing to individual railways by other concerns (e.g., for freight) are paid out

direct by these concerns to other parties without ever being entered in the railway administration's books. It is on this account difficult to accept the published figures of revenue and expenditure on the various lines at their face value. With the exception of the Peking-Suiyuan Railway, for a brief period in the summer, and of the Peking-Mukden Railway during the first six months of the year, the Chinese railways have been exceptionally free from interference caused by military operations or banditry.

205. In the first four months of the year considerable dislocation of traffic on the railways to the south of Peking, particularly the Peking-Hankow line, was caused by movements of troops concentrating on the old capital for the Jehol campaign. This was repeated with the withdrawal of the troops during July and August.

206. There has been a considerable extension of existing lines, and large schemes have been sanctioned for new construction. These developments have been embarked upon, however, without regard for (and sometimes in violation of) prior obligations secured on the railway earnings. Every single railway under Chinese Government control is still in default in respect of one or other of the charges secured on its revenues. In spite of occasional repayments made on some of the British loans, the load of indebtedness has steadily increased, and, generally speaking, it cannot be said that the situation shows any improvement from the point of view of the bondholders, though references in communications from the Chinese authorities to a "comprehensive scheme" for dealing with the problem have lately become rather more definite in expression, and there appears to be a clearer recognition in Government circles that the question calls urgently for practical measures of reform.

207. The Ministry of Railways itself has no effective control over the administration of the various lines. A scheme is said to be under consideration for converting the Ministry into a department of the Ministry of Finance, thus bringing it directly under Government control, with a view to co-ordinating and improving the administration of the railways. So far, however, the plea of centralisation has been used in practice merely as a pretext for diverting hypothecated funds to financing new construction, a purpose which is sometimes also excused by the Ministry of Railways on the ground that it is the only way in which these funds can be saved from the clutches of the military, who refuse to countenance their being used, as they properly should be, for the payment of debt.

208. The total amount which the Ministry of Railways have recently agreed to pay to the military authorities, after much grumbling on the part of the latter, is said to have been fixed at 400,000 dollars a month to Chiang Kai-shek, and 200,000 dollars to the Peking Military Council; the only sums known to be paid under this arrangement are 150,000 dollars by the Peking-Mukden Railway and 70,000 dollars by the Tientsin-Pukow Railway. The former line also pays 100,000 dollars a month out of its revenues towards a loan from Chinese banks for extension on the Lung-Hai Railway. When Mr. S. F. Mayers, the chairman of the British and Chinese Corporation, who has recently visited China, protested to the Minister of Railways against the latter appropriation, the Minister suggested an arrangement by which 60 per cent. of the railway's net earnings should be devoted to the Ministry's requirements and 40 per cent. to the corporation. A first payment of 440,000 dollars was made under this arrangement in October, and was devoted to payment of arrears of principal of the Shanghai-Hangchow-Ningpo Railway Loan.

209. No real attempt has yet been made to meet Government obligations in respect of railway loans. Claims on customs funds under the Hukuang and Tientsin–Pukow Railway Loan agreements have been recognised as valid by the Ministry of Railways, but the Chinese Government still declines to give effect to the relevant articles in the loan agreements. It is difficult to see how any Chinese Minister of Finance is going to find the 16 million dollars odd necessary for the yearly payment of these loans out of the scanty surplus customs revenues so urgently needed for purposes of general administration.

210. As regards the Hukuang Loan, a question has arisen between ourselves and the French on the one hand, and the Americans on the other, as to whether the 5 per cent. Famine Relief Surtax, on which the American Cotton/Wheat

Loan of 1933 (see under "Finance") has been secured as a second charge, forms part of the customs revenues on which the bondholders have a claim under article 9 of the Hukuang Loan Agreement: The Americans apparently take the view that this surtax does not form part of the increased customs revenue hypothecated under this article.

- 211. The vigorous representations on the question of railway indebtedness de by His Majesty's Minister in February, and again in October, were received by the responsible officials with an unusually candid admission of their appropriateness, and proposals for a joint conference of British and Chinese experts to discuss methods of payment met with quite a favourable response.
- 212. According to statements prepared by the Auditing Department of the Ministry of Railways, as published in the foreign press and not contradicted, the balance of the accounts of the fifteen Government railways for 1932 showed a loss of 1,096,332 dollars on the year's operation. In addition, military transport not paid for cost 8,276,463 dollars, while at a moderate estimate military subsidies may be put at 5 million dollars, making a total deficit for the year of considerably over 14 million dollars. As a result of this constantly increasing drain on its resources, it was estimated that the Ministry of Railways was saddled at the end of 1932 with a total debt of some 1.353,684,000 dollars.
- 213. So far as British loans alone are concerned, figures furnished by the British and Chinese Corporation show that on the 30th June, 1933, the total sterling indebtedness had increased since the same date in the previous year by £84,778, viz., from £11,243,372 to £11,328,151. The silver indebtedness had also increased, roughly to the equivalent of £434,600. To these sums must be added a figure of some £750,000 on account of the Peking Syndicate's Taoching and Chingmeng Railway Loans, giving the total outstanding on British railway loans alone at the 30th June last as some £12,500,000.
- 214. The debts on the German portion of the Tientsin-Pukow Railway Loans, and on the French, American and German portions of the Hukuang Railways Loan had, in addition, increased by over £600,000, thus automatically retarding the liquidation of the British portions of these loans.

Peking-Mukden Railway.

215. The Shanhaikuan incident of the 1st January determined the young marshal on a policy of resistance to Japan, and orders were immediately given for the concentration of rolling-stock at Fengtai, the junction on the Peking-Mukden Railway a few miles from Peking. Much of this rolling-stock was sent down the Peking-Hankow Railway to bring up the troops of Shang Chen, Sun Tien-ying and other generals. These movements continued until the middle of February, and only a passenger service was maintained. The sector between Chinwangtao and Shanhaikuan was considerably damaged for the pulling up of rails for making dugouts, while the bridge over the Sha Ho was partially destroyed by the Chinese. After the clearance of Jehol proper, the Japanese undertook an operation to drive out the Chinese from the passes in the Wall in the Luantung area, and to dislodge them from the Shih Ho position. Between March and May the Chinese determined to build a new line from Yangtsun to Lutai, to cut out Tangku and the protocol zone around Tientsin. To furnish material for this purpose they started pulling up the double track between Peitaiho and Changli. A few kilometres only were, however, lifted, and some kilometres of line constructed running east from Yangtsun. The scheme was abandoned with the further advance of the Japanese. When this took place (15th May) General Ho Chu-kuo, on his retirement, blew up one girder junction of the big Luan River bridge. The Japanese repaired this with sleeper cribs as a temporary measure, and a limited coal service was run to Chinwangtao after the signing of the Tangku armistice agreement (31st May). The Japanese made their main withdrawal from the mining area a fortnight later, but it was over a month before through passenger traffic was resumed. By the middle of August the Japanese had repaired the Luan River bridge, and relaid the double track up to Chinwangtao; the portion between Shanhaikuan and Chinwangtao remains single. The Feng-Shan (outside the Wall) section of the railway has continued to pay the comparatively small service (£7,000 a month) of the original Peking-Mukden Railway Loan, and has finally

liquidated the Double Track Loan of 1921, though under the terms of the arrangement with the Japanese for the rendition of the line to Shanhaikuan, the Tientsin Administration has undertaken to refund the whole amount contributed for the latter purpose (some £200,000) at the rate of about £4,700 a month over a period of five years. The British and Chinese Corporation have protested to the two administrations against this arrangement.

Peking-Suiyuan Railway.

216. During the revolt of Feng Yu-hsiang and Fang Chen-wu in the summer, the iron bridge east of Hsuanhua on the Peking-Suiyuan Railway was destroyed by the latter's troops on the 19th July. While Feng Yu-hsiang held Kalgan (till the 8th August) the railway from Hsuanhua to Paotou was milked by him.

Shanghai-Nanking Railway.

217. The Shanghai–Nanking Railway has in a large measure recovered from the damage suffered in the Shanghai incident of 1932. There have been no developments in connexion with the proposal for a new terminus at Shanghai, or for taking over the line to Woosung. As from the 1st October, 1932, 5 per cent. of the daily earnings of this line have been paid into a special reserve account with the Hong Kong and Shanghai Bank for amortisation purposes, to be increased from the 1st October, 1933, to 7½ per cent. (similarly, 10 per cent. of the daily earnings of the Shanghai–Hangchow–Ningpo Railway have been set aside to meet loan payments). Substantial payments have been made in respect of arrears due to net profit certificate holders (of whom the Chinese Government is one), and of the instalments overdue on the Rolling-Stock Hire Purchase Loan of 1929. Unpaid military transport on this line shows a great reduction compared with the two previous years, but non-payment remains a considerable source of embarrassment to the line. The Minister of Railways recently made a tentative suggestion to Mr. S. F. Mayers (see above) that the two Shanghai railways (this and the Shanghai–Hangchow–Ningpo line) should be placed under a local board of management consisting of three Chinese and two British members.

Tientsin-Pukow Railway.

- 218. An agreement was signed in February 1933 by the Minister of Railways and Mr. R. Calder-Marshall, the appointed representative of the British firms, who are creditors of the Tientsin-Pukow Railway in respect of materials supplied to the railway (see paragraph 263 of last year's report). Under this agreement the total indebtedness was fixed at £149,125 14s. 2d. and 8,085,193·77 Mexican dollars, to be repaid by a monthly minimum payment of 50,000 dollars. After payment of the first two instalments in February, these monthly payments were suspended. Three further payments have since been made, but up to date three monthly payments are still in arrears.
- 219. The long-overdue payments in respect of salary, &c., to British employees of this railway (see also paragraph 263 of last year's report) were liquidated in April last. The sums payable to the employees of the Canton-Hankow Railway, under the same arrangements, were allowed to fall into arrears during the year, but were finally wiped off in October, in response to His Majesty's Minister's personal representations to the Minister of Railways.
- 220. A ferry across the Yangtze between Nanking and Pukow, connecting the Nanking-Shanghai and Tientsin-Pukow Railways, was put into operation on the 22nd October. The ferry was built in Great Britain and paid for out of British Boxer indemnity funds. It arrived in China under its own steam in May, but could not be put into service till the terminal piers on either side of the river were completed. There is no saving of time on the journey between Shanghai and Peking, as the trains have to be divided into three sections before they are placed on the ferry, and the consequent shunting operations, &c., take longer than was previously required for the passengers and their luggage to change trains and cross the river. Coincident with the inauguration of the ferry, however, the journey between Shanghai and Peking has been speeded up some five hours and now takes roughly forty-five hours. It is reported that the Chinese Government intend to order an additional ferry for this purpose.

Lung-Hai Railway.

221. It is reported that the section of this line from Tungkuan to Sianfu is to be completed by June of next year; it is said to be 130 kilom. long, and is estimated to cost 13 million dollars, including locomotives and rolling-stock (the money is apparently to come from the earnings of other railways—see above). Work is also reported to have been started, in accordance with a contract signed with the Netherlands Harbour Works Company in May 1933, on the new harbour at Hsukow (Loyao), destined to be the eastern terminus of the railway on the sea coast; this place is 30 kilom. from the existing temporary terminus at Haichow, and was the site originally determined upon as the terminus of the line.

Peking-Hankow Railway.

222. A report by the chairman of the Railways' Improvement Commission gives a dismal picture of the state of this line. Of 2,400 freight cars, only 1,600 are fit for use, which is about 40 per cent. of the original number owned by the line; of 380 passenger cars, only 200 are fit for use, while of 200 locomotives, only 130 are serviceable, and these are very old, causing frequent accidents. There is no money to buy spare parts, while the tools in the railway's repair shops are out of date.

Hangchow-Kiangshan Railway.

223. It is said that this railway, which is operated as far as Kinhwa, has obtained a loan of $2\frac{1}{2}$ million dollars from Shanghai bankers for its completion to Kiangshan, on the Chekiang–Kiangsi border. It is hoped to inaugurate traffic as far as Kiangshan by the end of 1933. The line is said to have cost 14 million dollars. It is apparently intended to continue the line over the border to Yushan in Kiangsi, from which another railway is projected to Pinghsiang and Nanchang, to connect with the Canton–Hankow and Nanchang–Kiukiang railway systems.

Chengting-Taiyuan (Shansi) Railway.

224. This railway, formerly operated by the French syndicate, which furnished funds for its construction, was taken over by the Chinese in 1932. It was early in the present year ordered to contribute 100,000 dollars a month to the expenses of construction of the Lung-Hai Railway, to the prejudice of the Belgian syndicate, which holds a second mortgage on the line.

Canton-Hankow Railway.

- 225. The Boxer Indemnity Board of Trustees signed an agreement with the Ministry of Railways in July, under which they undertook to make a loan, when required, to the Ministry of £4,700,000 for the completion of the railway, the loan to include all materials purchased through the Purchasing Commission in London (see under Indemnities).
- 226. The construction of the southern section is making some progress, and it is estimated at Canton that the line will be completed within four years. The railway now runs to Lokchong, and a direct express service from Canton to Lokchong is being arranged. The section from Lokchong to Laipotau will not be open to traffic till the track is found to be perfectly safe.
- 227. A British firm, Messrs. Perrins (China) (Limited), who are associated with Belgian financial interests, have been allowed by the Ministry of Railways four months (from the 10th August to the 10th December) in which to complete a general and comprehensive tender for the completion of the Canton-Hankow Railway (the section from Lochang, in Kwangtung, to Chuchow, in Hunan, some 250 miles), during which period the Ministry undertakes not to negotiate with any other company for a general tender. The equipment required will have to be obtained through the Purchasing Commission of the Board of Trustees of the Boxer Indemnity Fund in London, who will issue specifications and invite tenders. The board of trustees have given their general approval to this project for the submission of a comprehensive tender, provided the terms arranged in no way conflict with the terms of the exchange of notes under which the indemnity funds are being remitted by Great Britain to China.

Canton-Kowloon Railway.

228. The Chinese section have again approached the British section with proposals for revision of the railway agreement. It will be remembered that the Chinese have always been dissatisfied with the agreement, which allots 65 per cent. of the through-traffic earnings to the Chinese section and 35 per cent. to the British section. At the request of the Governor of Hong Kong, informed enquiries were made at Nanking to ascertain the attitude of the Central Government towards the question and as to the appointment of negotiators on the Chinese side. The Waichiaopu have replied in an official note, stating that they have appointed a delegate to negotiate a settlement in consultation with the Kwangtung Provincial Government. The note enumerates the principal points for discussion, and requests the Hong Kong Government on its side to nominate its representative.

IV.—SHIPPING.

Shipping Regulations.

229. In May of this year certain regulations were promulgated by the Chinese Government entitled "The Provisional Yangtse Regulations, 1933." Though these regulations, for the most part, merely embodied existing practice, article 4 contained the statement that the Chinese Government reserved the right to close any of the treaty ports on the Yangtse. When the question of the possible unilateral closure of a treaty port under these regulations was referred privately to the Inspector-General, he said that it meant merely the withdrawal of customs facilities, and that at present the Chinese Government had no intention of closing any customs establishments. While it was not considered necessary in the absence of any specific case involving damage to British interests to make a formal representation to the Chinese Government, challenging the right to cancel unilaterally a stipulation of the treaties, His Majesty's Minister wrote a personal letter to the Minister for Foreign Affairs warning him that we reserved our treaty rights in the matters covered by these regulations. This attitude was approved by the Foreign Office.

230. It had been rumoured earlier in the year that the Chinese Government contemplated the abolition of the so-called inter-port duties, and the consequent closing of the custom-houses at certain of the smaller ports, which would mean that they would no longer be treated as ports of foreign entry. This proposal does not for the time being, however, appear to be a live issue, and however beneficial such a decision might be to the internal trade of the country generally (though possibly to some extent disadvantageous to the shipping companies having vested interests at the ports—especially river ports—from which customs establishments might be withdrawn), it is still unlikely that the Chinese Government will for the present be willing to forgo the considerable revenues derived from these duties.

Navigation Bureaux.

231. The establishment by the Chinese Government in July 1931 of Navigation Bureaux under the Ministry of Communications for the control of shipping (see section 256 of the report for 1931) has since that date given rise to attempts by the bureaux at various ports, particularly at Hankow, to exercise various forms of extra-treaty control over British shipping. These attempts have lacked uniformity, and have not been pressed very hard. Communications were, however, received from the Waichiaopu in October 1932, and again in March 1933, asking that British firms be instructed to comply with the requirements of the bureaux in regard to survey and measurement. No reply was sent to the first of these communications, but on receipt of the second it was decided that His Majesty's Minister's personal representative at Nanking should explain the standpoint of this Legation verbally to the Waichiaopu. This Mr. Ingram did in May last, pointing out that while we were prepared to acquiesce in the survey (though not registration) by the Navigation Bureaux, acting in lieu of the Maritime Customs, of British vessels engaged in inland water navigation under the Inland Steam Navigation Regulations of 1898, provided the bureaux carried out their functions in a reasonable manner under uniform legislation and on the understanding that British measurements were as far as practicable accepted, it was not possible for other classes of British vessels (whether ocean, coasting

or river steamers) to comply with the requirements of the bureaux, since the conditions as regards survey, &c., affecting such vessels, were governed exclusively by British legislation in accordance with the treaty position; and these vessels could not be subjected to any form of extra-treaty control, except as the result of international agreement. These views were subsequently embodied in a personal letter written by Mr. Ingram to the head of the European and American Epartment of the Waichiaopu, while a letter in similar terms was addressed to him by the counsellor of the United States Legation, who had been associated with Mr. Ingram's verbal representations.

Pilotage.

- 232. At the end of November the Shanghai General Chamber of Commerce received a letter from the Coast Inspector transmitting copies of new *Provisional Pilotage Regulations* promulgated by the Chinese Government, under which all pilotage organisations at the coastal and river ports were to be taken over by the Chinese Government and a new pilotage authority constituted to take the place of that authorised by the General Pilotage Regulations of 1868. The chamber were asked to furnish the name of their representative who would sit on the new Pilotage Board. To this the chamber replied that as the matter was one affecting foreign treaty rights the whole question would have to be referred to the consular body, and until the latter had had an opportunity of discussing the situation the chamber were unable to furnish the name of a member to represent them on the new Pilotage Board. Copies of the correspondence were forwarded to the senior consul by the chamber with a covering letter drawing attention to various objectionable features in the new regulations and recommending that if the Chinese Government were not able to frame regulations which would be acceptable to the shipping companies, the present Pilotage Service Regulations should be continued.
- 233. It is unnecessary here to discuss the new regulations in detail, but it may be mentioned that they deliberately exclude the recruitment of any new foreign pilots, while they make no provision whatever for the protection of the interests of the existing pilots which, in Shanghai at any rate, are very considerable. Moreover, the composition of the new Pilotage Board is such that in spite of the fact that the Inspector-General of Customs recently informed His Majesty's Minister that the control of pilotage matters was to be in the hands of the customs, the representation of that department are outnumbered by those of other Government departments.
- 234. The matter was discussed by the consular body, which endorsed the attitude adopted by the chamber. It was agreed that identic letters be sent to the Commissioner of Customs and the Mayor of Greater Shanghai. In these the consular body stated, *inter alia*, that they could not approve of the application to ships of their nationalities of other pilotage regulations than those which in the past had been made in mutual agreement by the consuls of all nations and the Chinese authorities unless such modifications or innovations as may be desirable are approved by all parties concerned.
 - 235. It remains to be seen what effect these representations will have.
- 236. The question of a possible increase of Chinese tonnage dues is referred to in the section on customs and tariffs.

V .- FINANCE AND TAXATION.

237. The Minister of Finance has not at the time of writing published his report for the fiscal year ending the 30th June, 1933 (see section 181 of last year's report). There are, therefore, no authoritative statistics available on which to base an estimate of the present financial position of the Chinese Government. Generally speaking, the situation is very much what it was a year ago, at any rate from the point of view of the foreign investor in Chinese securities. Loans secured on the customs revenues have been punctually met, while the railway loans and other unsecured obligations of the Chinese Government are still heavily in default (see also under Railways).

238. At the end of October, not much more than a month after his return from his trip abroad (see below), the Minister of Finance, Dr. T. V. Soong, generally regarded as the strongest and ablest personality in the Nanking Government, resigned, and was succeeded by his brother-in-law, Dr. H. H. Kung, another member of the "Soong dynasty," and former Minister of Industries. It is not generally known how far Dr. Soong's resignation was due to differences of opinion with his colleagues over their policy of closer rapprochement w. A Japan, or how far it was due to his unwillingness or inability to meet his brother-in-law, General Chiang Kai-shek's, incessant demands for funds to prosecute his campaign against the Communists in Central China. In any case, the Government was reported to be facing a monthly deficit of over 10 million dollars a month, chiefly, if not entirely, on account of this expenditure, and of their advances to the Northern Political Council at Peking, and Dr. Soong may have felt that his only means of effective protest against this reckless finance was to resign. Opinions in Shanghai are divided as to whether his action was on this occasion, as so often previously, a case of "reculer pour mieux sauter," and whether he will come back in the near future or not. Shortly before he left the Ministry of Finance, Dr. Soong arranged for the flotation of a loan of 100 million dollars Treasury bonds, secured on the surplus customs revenues, for the purpose, it was reported, of repaying advances made by the Shanghai bankers to the new Government.

239. On assuming his post, the new Minister of Finance made a statement to the effect that the Government's revenue for the year 1933 was estimated at 680 million dollars and expenditure at 800 million dollars, leaving a deficit of 148 million dollars or 12 million dollars a month, and added that the present monthly deficit was probably even larger than that.

240. With the incidence of the Fukien rebellion, there are at the moment of writing many signs that the Government is sorely pressed for funds, and that every possible method, including further and more widespread tariff increases, will be adopted to raise funds.

Visit of Minister of Finance to the United States of America and England.

241. Dr. T. V. Soong left China in April for America, accompanied by a large staff. His objects were said to be to ascertain the attitude of the United States Government towards the Manchurian problem, to explore the possibility of obtaining a loan from the United States (see Cotton/Wheat Loan below), and to investigate the situation in regard to the stabilisation of silver. He subsequently went to London to attend the World Economic Conference, and during June and July got into touch with leading financiers and industrialists in England, as well as with members of the Government, in order to expound his views on the economic reconstruction of China, and to seek financial assistance in prosecuting various extensive schemes of reform. He spoke of placing orders to the value of £8 million in the United Kingdom, provided credit terms could be arranged through the Export Credits Guarantee Department. The orders he had in mind were chiefly for 600,000 spindles, to enable the Chinese cotton mills to spin the finer yarns (and thereby compete better with Japan), for rails and rolling-stock for the Hukuang and Lung-hai Railways, for eight river vessels of some 2,000-3,000 tons, and six to eight coastal vessels of similar size to be assembled in China, and for plant for the development of the iron and steel industry in China. No decision was reached on these proposals owing to their indefinite nature and the absence of any offer of reliable security. Dr. Soong also suggested the establishment of an International Corporation, the capital to be subscribed partly from Chinese and partly from foreign sources, and with purchasing agents (Messrs. Kuhn Loeb and Co. in New York, and Messrs. Lazard Brothers in London, have already actually received such appointments) in the various countries participating, which was to be an instrument for the economic development of China, with aims similar to that of the existing consortium, but excluding the Japanese. Alternatively, he proposed to set up a consultative committee in London, to draw up some sort of a programme for the economic development of China, composed of representatives of the United States of America, the United Kingdom, France, Italy, Belgium, Germany and China, with M. Jean Monnet as chairman. Sir C. Addis and Mr. T. W. Lamont, representatives respectively of the British and American groups in the existing

China Consortium, were invited to serve on this committee. These invitations were not accepted owing to the very definite opposition of the Japanese group to the formation of any such committee without Japanese participation. Dr. Soong also extended an invitation to Sir Arthur Salter and M. Monnet to visit China before the end of the year, to draw up a report on the reconstruction work that should be undertaken, for submission to this proposed committee. hese gentlemen arrived in China in November, subsequent to Dr. Soong's resignation.

American Wheat and Cotton Loan of 1933.

242. In May 1933 Dr. Soong, the Chinese Minister of Finance, negotiated with the Reconstruction Finance Corporation, an instrument of the United States Government, a loan to the Chinese Government of 50 million gold dollars, to be expended in the purchase of wheat and cotton owned indirectly by the American Government. One-fifth of the total loan was to be spent on wheat, and the remaining four-fifths on cotton. The money was to be furnished by the United States Treasury, the rate of interest to be 5 per cent., and the repayment to be spread over three years. The procedure in regard to the wheat purchases was expected to follow that of the 8 million dollar wheat loan, previously made in September 1932. The Chinese Government was to sell the cotton to the Shanghai mills, and retain the proceeds until required for the repayment of the loan. security was to be the excise tax on rolled tobacco, flour, cotton yarn, matches and cement, which in 1932 had produced 22 million dollars (it was afterwards learnt that the loan was also secured, as a second charge, after payment of the original wheat loan of 1931, on the 5 per cent. Flood Relief Customs Surtax). As the transaction involved no public issue of bonds, it could be held not to infringe the actual terms of the China Consortium Agreement, in which the American group, with the full support of their Government, participated, though it was scarcely possible to reconcile it with the general aims of the consortium. It was defended by the Reconstruction Finance Corporation on the ground of its humanitarian motive, though such an argument was difficult to sustain, in view of the fact that four-fifths of the loan was to be expended on the purchase of cotton, and that the Chinese Government was free to dispose of the proceeds at it pleased. The other members of the Consortium group were also concerned at the hypothecation of so large a sum as 22 million dollars out of the general revenues of the Chinese Government. His Majesty's Government did not, however, for various reasons, see fit to make any representations in regard to the terms of the agreement. loan was the subject of much hostile criticism, both in China and abroad, as being designed solely to benefit the American cotton and wheat growers, and as being economically unsound from the Chinese point of view; it was also said that it would paralyse the normal channels of trade and sources of production in China, and that the proceeds would be diverted to the furtherance of political strife. The first objection was seen to be justifiable when the initial instalment of the cotton purchased from America under this agreement arrived in Shanghai, for, after unsuccessful attempts to find a buyer, the Minister of Finance was reported to have sold the cotton to the local Japanese mills at a considerable discount, though this report was later denied by Dr. Soong. The latter has repeatedly declared that the proceeds of the loan will be devoted to reconstruction work and placed at the disposal of the National Economic Council, of which he has remained a member after his resignation from the portfolio of Finance.

The Customs Revenues and their Disposal.

243. A very confidential statement obtained from the Customs shows that, after providing for the service of all foreign and domestic loan and indemnity instalments, a balance of roughly 35 million haikwan taels was remitted to the Minister of Finance for the year 1932, out of a total revenue of 218,856,957 haikwan taels, including flood relief and revenue surtaxes. A further sum of nearly 10 million haikwan taels was paid to the Minister of Finance, representing the American and British portions of the Boxer indemnity for the period March-December 1932.

244. In spite of shrinkage in the import and export trade during 1933, as compared with 1932, the gross revenue of the Customs was 9 per cent. greater for the period January–September than for the corresponding period of 1932,

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owing to the increased duties which come into force on the 22nd May (see under Tariffs). In October there was, however, a further shrinkage of trade, and it is anticipated that the total customs revenue for the whole of 1933 will be slightly less than for 1932.

Abolition of the Tael.

- 245. The Central Mint at Shanghai was officially opened on the 1st Marc to mint new standard silver dollar coins, in anticipation of the abolition of the tael as a unit of national currency. Regulations governing the coinage of the new unit (dollar) were adopted by the Legislative Yuan on the 3rd March, and on the 10th March the tael was declared to be officially abolished. According to these regulations, each was to be convertible into the other at the fixed rate of 100 dollars equals 71.5 taels; in this way it was hoped that the tael would gradually disappear, since there would be no further object in retaining a unit of currency whose conversion from or into dollars no longer afforded a source of profit. After the 10th March all customs export and interport duties had to be paid in standard dollars instead of haikwan taels, though import duties and other gold unit levies remained unaffected. The new rate laid down for payment of tonnage dues on vessels over 150 tons represented an increase of 4.125 per cent. over the old rate, and that on vessels under 150 tons a decrease of about 3.9 per cent. The regulations stipulated that the new dollar was to be 88 per cent. silver and 12 per cent. copper, and there was a fear that provincial mints might resume the minting of silver dollars with a smaller silver content, reminting the standard dollars for this purpose, and thus gradually causing the latter to disappear. Against this, however, there were huge stocks of bar silver in Shanghai available for minting purposes, while Shanghai, with its large supplies of silver bullion, must always be the controlling factor in the national currency supply. The new dollar was to bear on its face a likeness of Dr. Sun Yat-sen, with a sailing boat on the obverse. A Sino-foreign supervisory committee was appointed to supervise the operations of the mint and to ensure the maintenance of the standard fineness of the new dollars.
- It was understood at first that there would be a transitional period of from four to six months, during which taels and dollars would continue to operate side by side at the fixed rate of 71.5 until the tael automatically disappeared from use. An order was, however, issued by the Ministry of Finance on the 5th April, and adopted by the Central Political Council the following day, declaring that after the 6th April all business transactions must be in silver dollars, and that those in taels would be considered illegal. A duty of $2\frac{1}{4}$ per cent. was also decreed on the export of silver bars, &c., with the object of balancing the minting charge of 24 per cent. Both the Shanghai Chinese banks, which had hitherto opposed the measure, and the foreign banks, which had sympathised with it, supported the change, though they were put into a difficult position by the suddenness of the Government's decision. The foreign banks decided that there could be no compulsory conversions of tael accounts into dollars, but that these should be at the option of the client, and take place gradually as opportunity offered; no new tael accounts would be opened, however, and the tael-dollar exchange maintained at the fixed rate of 71.5 without any charge for commission (a charge of 10 cents commission for buying and selling transactions had been made when the regulations were first promulgated in March). After the 10th April the foreign exchanges were also quoted by the foreign banks in dollars.
- 247. As long as the standard dollar is maintained at the stipulated silver content of 23·493448 grammes of pure silver, all will be well, but if dollars with a lower silver content oust the standard dollar from circulation, or if the silver content of the latter is reduced for any reason, then the standard unit of currency may again become not a coin, but a definite weight of silver, as with the tael. Generally speaking, it may be said that the tael is now dead as a unit of currency, and the complete discontinuance of its use is only a matter of time.

Internal Taxation.

248. Mr. Hsieh Chee, the Director of Inland Revenue, informed His Majesty's Minister in October that, by abolishing as far as possible the practice of farming local taxation, having all provincial taxes remitted direct to the

Central Bank and allowing the local authorities a monthly sum equal to, or even greater than, the net amount previously collected, he had managed to secure control of the total revenues by Nanking and at the same time to satisfy the local authorities. He said that the net consolidated tax revenue now amounted to 110 million dollars, of which the cost of collection was 3·4 per cent. Certain regions still presented problems of taxation, e.g., the Hankow business tax, which low seemed to have developed into a commodity tax, and the Canton taxes on kerosene oil, but, generally speaking, the local authorities were being kept quiet by dint of a monthly grant from the National Exchequer. While allowance must be made for a perhaps pardonable degree of exaggeration in this statement, there is little question that considerable progress has been made with the centralisation of internal taxation under the Ministry of Finance, especially as regards those provinces which are genuinely, and not merely nominally, controlled by the Central Government at Nanking. It is, however, scarcely true of the outlying provinces, such as Szechuan and Yunnan, or of the Province of Fukien, which is continually at loggerheads with Nanking over the monthly remittances, and is always taking the law into its own hands in imposing additional forms of taxation not sanctioned by the Ministry of Finance. The principal taxation questions with which the Legation has had to deal during 1933 are those outlined below.

Taxation of Oil at Canton.

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249. In January 1933 the Ministry of Finance at Nanking sought to introduce a heavier duty on imported crude oil. This action was stoutly resisted by the native refineries at Canton, which had been established in the previous year for refining crude oil imported from the Dutch East Indies. The oil so refined was steadily pushing the imported products of the foreign oil companies out of the market, and the annual loss to the customs revenue for Kwangtung Province alone was placed at half a million taels. The interests of the Nanking Government and the foreign companies were thus identical, but members of the Canton local Government were largely interested in the new refineries, with the result that the South-West Political Council refused to allow the customs to collect the higher duty on crude oil, and the foreign companies were forced to import crude oil and establish their own distilleries. This was a comparatively simple matter, and was effected so rapidly that twenty out of thirty-five local distilleries were soon put out of business, and the remaining fifteen were being run at a loss. Thereupon the South-West Political Council issued regulations entitled "Provisional Regulations for the Establishment of Factories," making it impossible for the foreigncontrolled companies to establish factories in Kwangtung; under these regulations all factories had to register, and permits to import crude oil could only be granted to factories so registered. A further set of regulations issued simultaneously provided for the establishment of an office called the Special Liquid Fuel Registration Bureau, the functions of which were to issue permits for import of fuel oils: without such permits it was impossible to obtain release of the oil from the customs. The grant of these permits was, however, confined to registered manufacturers, and, as stated above, only Chinese-controlled factories could obtain registration under the new Factory Regulations. The foreign companies were, therefore, prevented from obtaining permits to import crude oil, while their dealers were prevented from marketing locally-distilled foreign brands of oil, on the ground that these brands were not registered. When the question of this obvious contravention of treaty rights was taken up by the British and United States consuls-general, the Canton authorities exhausted all conceivable arguments, with a view to postponing the issue, over the precise form of registration, to which the foreign companies were to be made to conform. The conditions insisted upon included a promise to "obey the factory law and rules pertaining to the registration of factories, and all other laws enacted in regard to public order, hygienic conditions and regulation of output, and to pay the business tax." These conditions were clearly incompatible with extraterritorial status and treaty rights, while the regulation of output was regarded by the foreign firms as highly dangerous, because the native factories would exaggerate their output in order to obtain a larger quota. Finally, it was suggested by the Canton authorities that, instead of revising the form of application for registration, there should be an exchange of notes making it clear that foreign firms would not be expected to conform to regulations incompatible with

treaty rights, that they would not be required to submit to limitation of output, and that the so-called "business tax" would be defined as referring exclusively to a non-discriminatory tax per unit of locally-refined kerosene. A formula for the proposed exchange of notes was finally agreed upon to the effect that the Canton authorities "had no idea of proclaiming or enforcing against British firms laws and regulations governing oil factories which were in contravention of the treaties in force." The foreign oil companies were accordingly advised that they might apply for registration under these conditions, which, it was hoped, would obviate further trouble. As the Canton Administration were also proposing to impose a tax of 3 dollars a case, both on imported and on locally-refined oil, the acting consul-general, in his note to the Inspector-General of Foreign Affairs, added that "the question of collecting from retailers an additional tax, so far as it concerns imported kerosene, has no bearing upon the question of the registration of British oil companies, and I reserve the right to make representations in regard thereto as a separate issue." The attitude of the acting consul-general towards the imposition of such a tax on locally-refined oil was that there was no ground for objection, provided there was no discrimination, but that such a tax on imported oil was contrary to the assurances given by the Minister of Finance to the oil companies in 1931, and to the spirit of the tariff autonomy treaties. A similar tax of 1 dollar per unit has for some time past been collected by the Fukien provincial authorities, who have disregarded the instructions of the Ministry of Finance to cease collecting it.

Business Taxes.

250. The local authorities at Canton, Swatow, Hankow and other ports have continued to urge His Majesty's consuls to instruct British firms to pay the business tax. The Nanking Government decided to put an end to the practice of farming out this tax at Hankow and to send their own appointees to the Business Tax Bureau at that port to levy the tax in the guise of a tax on various commodities of export, such as wood-oil, hides and skins, tea, &c., through the medium of the Bureau for the Testing and Inspection of Commercial Commodities. After the enforcement of the tax on wood-oil had been postponed for two months as the result of representations made locally by the consular representatives, it was decided to drop any opposition to this tax, in the hope of thereby staving off the more objectionable forms of business tax proper based on capital or turnover, with its unpleasant features of inspection of firms' books, &c., and to confine the payment of the tax to specified goods. Subsequently, taxes of this nature were collected on tea, and hides and skins, as well as wood-oil, but in each case they were not unreasonable in amount.

VI.—TRADE.

- 251. As these notes on trade have necessarily had to be prepared in advance of the end of the year, it is impossible to give any figures beyond those for the first ten months of 1933.
- 252. A report by the commercial counsellor to His Majesty's Legation on trade and economic conditions in China up to April 1933, which will have been published before this report goes to the printers, gives a comprehensive picture of China's trade with the rest of the world during the present century, and particularly during the past four years, 1929–32. It is a striking fact that, in 1929, before the world trade depression set in, the total foreign trade of China accounted for only 2·12 per cent. of the total trade of the world, though the country contains roughly one-quarter of the world's population. The value of the import trade increased by five times between 1900 and 1931, but native industries cannot be placed on a firm footing till security is established. In 1932, in a country whose strength should rest in her agriculture, no less than 20 per cent. of her imports were of wheat and rice, and another 10 per cent. of sugar and other food-stuffs. China yearly faces a serious adverse balance of trade, for which existing exports can in no degree be held to compensate. In 1932, the value of exports was but little more than half the value in 1931, and for the first ten months of 1933 the value was over 20 per cent. less than in the corresponding period of 1932. The adverse balance of trade for the first six months of 1933 was no less

than £30 million, and may be as much as £50 million for the whole year. Two-thirds of the total exports in the first six months of 1933 were required to pay for the wheat and rice imported during the same period. Unless this rapidly increasing tendency is checked, it seems that China must cease to be a factor of importance in the trade of the world.

China, however, is bent on the improvement of her industries, and it only needs reasonable security to make this possible. The total exports of manufactured goods in 1932 were valued at 51·3 million haikwan taels, of which cotton piece-goods accounted for 10·7 million. The cotton industry is the leading factory industry in China to-day, and the decline in imports under this heading is largely due to the increasing volume of native-manufactured cloths-thus the imports of cotton piece-goods in 1932 was only 40 per cent. of the value of similar imports in 1929, a 60 per cent. decline in four years. The recent increases in the tariff (see under Tariffs) should also do something to foster local production, though it is to be questioned if these increases have been imposed as much with a view to protection of native industries, as with the idea of a quick increase in revenue returns. What China chiefly needs is capital equipment in the shape of railway, public utility and factory (particularly textile) equipment, highway transportation equipment, aircraft, and river and costal vessels. In the four years 1929 to 1932, the share of the United Kingdom in the import trade with China averaged from 8 to 11 per cent., though that of the British Empire as a whole averaged 35 per cent. The two most important countries trading with China are, however, Japan and the United States of America; Japan, owing to the suitability and cheapness of her merchandise and her proximity to the market; and America by reason of her cotton, wheat, timber, oils and motor vehicles. Moreover, the imports from these countries are greatly assisted by the fact that they are by far the largest markets for Chinese produce. Together, they take normally 40 per cent. of China's exports. The trade between the three countries, all bordering the Pacific, is rapid, natural and easy, as compared with trade between China and European countries, an advantage which applies particularly to consumable goods, raw materials, and food-stuffs. The import of high-grade consumable goods from the United Kingdom is bound to be limited for some time to come owing to the infinitely lower manufacturing costs in oriental countries. All the leading manufacturing countries now realise that the best outlet for their capital goods lies in the establishment of manufacturing enterprise in China, and that participation in such undertakings can only be secured through co-operation with the Chinese. There has been much talk during the year of the establishment of large-scale factories in China for aircraft (American), steel products (German), and sulphate of ammonia (joint British and German), with a mixture of Chinese and foreign capital and foreign technical assistance. Contracts for the first two enterprises are believed to be on the point of signature as these words are written. The outstanding weakness which handicaps all such development is the fact that the Chinese Government, in allowing defaults on her railway obligations to reach unmanageable proportions, has broken faith with the foreign investors who so confidently provided her in the years before the Great War with the means of initiating a sound system of communications.

254. Expressed in silver (which is probably the truest criterion), the total of China's foreign trade reached its zenith in 1931, when it amounted in value to 2,342 million haikwan taels (£180 million). The sterling value of the trade in 1922, when silver was at a very considerable premium, was, however, £300 million. In 1932 the value of the trade had dropped to 1,542 million haikwan taels (£125 million). The reasons for this large drop were not so much the world-wide trade depression, but largely internal causes, of which the outstanding factors were the anti-Japanese boycott and the loss of the Manchurian trade.

255. Figures of *imports* into China from abroad for the first ten months of 1933 give a total of 1,158 million Mexican dollars, as compared with 1,405 million for the corresponding period of 1932, a drop of 17.59 per cent., though the drop is smaller expressed in terms of gold. The decrease is heaviest in raw cotton and cotton piece-goods of all descriptions. The United Kingdom share shows a slight increase as between these two periods of from 11.35 per cent. to 11.52 per cent. The share of the United States of America fell from 25.49 per cent. to 21.35 per cent., or 4.34 per cent., while the Japanese share

fell from $14\cdot 20$ per cent. to $9\cdot 32$ per cent., or $4\cdot 88$ per cent., and the German share increased from $6\cdot 77$ per cent. to $7\cdot 81$ per cent., or $1\cdot 04$ per cent. These percentages mean a shrinkage in British trade of £2 million, and in Japanese trade of £6 million roughly.

256. The total net *imports and exports* for the first ten months of 1933 were 1,665 million dollars, as compared with 2,061 million dollars for the corresponding period of 1932, a drop of about 19 per cent. Exports alone for the same period were 507 million dollars for 1933, as compared with 656 million dollars for 1932, a drop of roughly 21 per cent.

257. At the moment of writing (early December) it is anticipated that owing to the higher duty rates the customs revenue for 1933 may possibly exceed that for 1932 by some 10 or 15 million dollars (compare statement in section under Finance). Such a result will, nevertheless, represent a considerable shrinkage in the total external trade of the country.

VII.—CUSTOMS AND TARIFFS.

Fining of British Ships.

258. The question of the fining by the Chinese Customs of British ships for smuggling (see section 213 of last year's report) continued to be a subject of discussion in semi-official correspondence between His Majesty's Minister and the Inspector-General of Customs. It was pointed out to the latter that the system of enforcing payment of fines by administrative action, based on the annual guarantee bonds," had no treaty basis, but had been acquiesced in by the British shipping companies, who trusted in the fairness of the customs authorities; the Customs had in fact no legal treaty right to fine a British vessel or merchant at all without the intervention of the British authorities. Sir Frederick Maze replied, not seriously contesting the treaty position, but maintaining that the situation had been modified in recent years by the recognition by the Powers of China's increased authority in customs and tariff matters, and that the Powers had tacitly accepted new regulations promulgated by the Chinese Government, affecting customs practice and procedure, which tended to curtail the privileges formerly enjoyed by foreign merchants trading in China. He promised, however, to instruct the Commissioners of Customs to exercise greater moderation in the infliction of penalties, and the question was left at that

Examination of Firms' Books by Customs.

259. Under the tariff, Rule I, as revised in 1929, the Customs had claimed the right to inspect firms' books to determine the duty-paying value of goods on importation. In April 1933 the Customs at Shanghai issued a notification not only reasserting this right, but also claiming authority to take similar action in the case of duty-paid goods already imported, to determine whether the correct duty had been paid. Such action had, in fact, already been taken in the case of certain foreign firms which had defrauded the Customs by declaring their goods at too low a valuation, and which had as the result paid without protest considerable fines. The consular body considered that the authority claimed by the Customs in the notification in question was contrary to treaty and extraterritorial rights, and wrote to the Customs asking under what Chinese law they were empowered to take such action. The reply stated that the notification was issued on the instructions of the Central Government, with whom the matter should be taken up if so desired. The unhelpful nature of this answer caused certain members of the consular body to infer that the Customs wished to abandon the time-honoured practice of direct communication between the Customs and the consular body, and the senior consul referred the question to the Diplomatic Body. His Majesty's Minister held that the question of direct communication with the Customs was a side-issue, and that the complaint that the Customs wished to abandon this practice was based on insufficient evidence. As regards the inspection of firms' books, with a view to ascertaining duty-paid value at time of importation, the matter had already been thrashed out in 1929, when the claim to do this was first made by the Customs, and since it did not then appear

that any actual treaty rights were thereby infringed, and since the Customs had given assurances that there was no intention of applying the new rule rigorously in all cases, no protest had been made. With this decision His Majesty's Government in the United Kingdom had concurred at the time, and the claim to this right had remained unchallenged. The United States Government now, however, took the view that the practice was contrary to treaty rights, and were willing to protest. His Majesty's Minister considered that there was a practical distinction between this claim and the further claim to inspect books after duty had already been paid, as in the former case the Customs could enforce their will by refusing to allow the goods to be imported, whereas the exercise of the latter right might entail some positive action contrary to treaty rights. Fundamentally, there was, however, little distinction between the old claim and the new, since in neither case could the inspection of books be carried out without either the acquiescence of the firm concerned or the order of a competent court. His Majesty's Minister, while agreeing with his American colleague that any improper attempt to enforce the asserted right would be a contravention of the treaties, took the line that it was unnecessary to press the matter further. The question was reported to the Foreign Office, with a request for instructions as to whether, should disputes arise in the future over the inspection by the Customs of the books of British firms, His Majesty's Minister would be justified in insisting that the machinery for arbitration provided by the tariff rules attached to the treaty of 1902 should be set in operation, or whether we should acquiesce in the claim made by the Customs in 1929 of the right to settle the dispute themselves in accordance with the provisions of the present rule, including the inspection of firms' books, as long as no positive action was taken to enforce such inspection against the wishes of the firm concerned, or in contravention of their extra-territorial rights.

Tonnage Dues.

260. The Inspector-General of Customs informed the commercial counsellor confidentially in August that the Chinese tonnage dues were shortly to be increased. No steps have, however, as yet been taken to that effect.

Smuggling from Hong Kong into China.

The smuggling of goods from Hong Kong into China continues on a large scale. The constant increases in the Chinese tariff, the existence of a free port so close to the coast of China, the interest of high officials of the Canton Province in the smuggling, all contribute to the perpetuation of this evil. On the 5th December, 1932, the Hong Kong Government issued an ordinance prohibiting the import and export of unmanifested cargo, and exacting considerable penalties for infringements. The efficacy of this legislation was, however, criticised by the Inspector-General of Customs on the ground that it placed on the agent or master of the ship concerned the duty of detecting the presence of contraband on board, without the intervention of the Hong Kong officials. After discussing the question with the Governor of Hong Kong in January last, on his return to China, His Majesty's Minister broached the subject of the abortive customs agreement with the Canton authorities, but was unable to accomplish very much owing to the interests of the Cantonese officials (the brother of Marshal Chen Chi-tang in particular) in the smuggling trade. Sir Frederick Maze also took up the question at Canton early in the year, and afterwards told the Governor of Hong Kong that there was but little hope of the agreement being signed by the Chinese in the near future. Reports from His Majesty's consular officers at Canton, Swatow and Amoy indicate that there is a regular system of selling goods "ex godown Hong Kong" for delivery in China at an inclusive charge of 10 per cent. of the value of the goods as declared to the agents of the smuggling organisation in Hong Kong. The proportion of seizures is not sufficient to prevent this from being a very lucrative business. The goods chiefly smuggled are those of small bulk, on which the import duty exceeds 12½ per cent., e.g., thread, sugar, woollen goods. Contraband traffic is chiefly by junk, so that British shipping companies are for the most part not implicated. The principal need is for adequate preventive measures, since the rocky, indented coast of Kwangtung Province offers an exceptionally favourable field for smuggling operations. Both Macao and Formosa are implicated, so that the [9914]

whole blame cannot be thrown upon Hong Kong. No real remedy exists if the Cantonese authorities persist in their refusal to co-operate in passing the customs agreement.

Customs 5 per cent. Flood Relief and 5 per cent. Revenue Surtaxes.

262. These two taxes were originally a single surtax, called the 10 per cent. flood relief surtax, introduced on the 1st December, 1931, for eight months; had originally been intended to reduce it to 5 per cent. on the 1st August, 1932, though at that date the Chinese Government decided to maintain it at 10 per cent., but in two parts. The 5 per cent. flood relief surtax was to continue until the American wheat credit of 1931 had been liquidated (apparently till the end of 1936), while an additional surtax of 5 per cent. (now called the revenue surtax) was introduced, to have effect for not more than one year, as a special surtax to assist in meeting the deficit from the loss of the Manchurian revenues. This latter surtax, which should have terminated on the 31st July, 1933, has been renewed for eleven months and is to remain in force until the 30th June, 1934.

263. All imported articles exempted from payment of these surtaxes under the exchange of notes attached to the Sino-Japanese Tariff Agreement of May 1930 are now subject to these surtaxes.

Marking of Goods Regulations.

264. In December 1932 the Chinese Government promulgated regulations providing that all goods imported into China must bear in Chinese characters the name of the country of origin, to come into force on the 1st August, 1933. The regulations were clearly hastily devised, and did not take into proper consideration the difficulties of marking certain classes of goods, or make adequate provision for exemptions. At the request of the British interests affected, His Majesty's Minister requested the Chinese Government to permit the use of English in place of the stipulated Chinese characters for marking the country of origin, and to postpone the enforcement of the regulations till the 1st January, 1934. In April a Customs notification was issued postponing the enforcement of the regulations accordingly. Certain tables were also issued amplifying the original regulations in regard to the marking of particular classes of goods. In May an amendment of the regulations was promulgated to the effect that the language of the country of origin might be used for marking goods. In spite of these amendments, however, the terms of the regulations gave rise to numerous representations on the part of British interests, while it is understood that strong objections were raised by the Japanese. Finally, a Customs notification was issued in November that enforcement would be further postponed for six months, i.e., until the 1st July, 1934.

Chefoo Breakwater Scheme.

265. By arrangement between the Chinese Government and the Diplomatic Body, the Chefoo Harbour Commission, consisting of five persons—the Superintendent of Customs (ex officio chairman), the Commissioner of Customs (ex officio treasurer), the senior consul, the chairman of the Chinese Chamber of Commerce and the chairman of the Foreign Chamber of Commerce—was formed in 1913 to carry out a scheme for the construction of a mole and breakwater in Chefoo harbour. Port surtaxes were levied, a grant of 10,000 taels a year was promised by the Chinese Government and work on harbour improvement was begun. Unable to float any loans during the Great War the commission afterwards got into financial difficulties, and in 1918, again largely through the exertions of the Diplomatic Body, a loan of 2 million taels was made to it out of customs revenues. In 1932, when this loan, with interest, amounted to some 4 million taels, the Minister of Finance called for repayment in a manner which would swallow up the commission's balance in hand and cripple its activities in the future, though work on the harbour was by no means complete. It was felt that the time was past when the Diplomatic Body could properly intervene, and that the Harbour Commission must make the best terms it could with the Customs. The commission stoutly resisted the demand, and as a result the Minister of Finance sanctioned an arrangement whereby the whole interest on the loan was to be remitted, and a sum of 80,000 Shanghai taels paid over in

July of each year by the commission in repayment of the loan. During the past year and a half much controversy has raged at the port and in the commission itself as to how the considerable balance in the hands of the commission should be spent in improving the harbour. The merchants of Chefoo, who are principally Chinese, are supposed to favour a scheme for the provision of additional berthing facilities, which will attract a larger amount of ocean shipping. The coastal hipping companies (amongst whom the British companies are prominent) say that the provision of such facilities is useless until there is a railway connecting the port with the interior (of which there is at present little prospect), and that the money can much more profitably be spent in dredging and similar improvements to the harbour. A contract with the Netherlands Harbour Works Company for the construction of additional berthing facilities was signed in January 1933 by three members of the commission, viz., the American and senior consul, the Acting Commissioner of Customs (a Dutchman, since transferred from the port owing to his part in these proceedings) and the chairman of the Foreign Chamber of Commerce (a German, whose place has since been taken by a British subject). The conduct of this transaction by the commission met with strong opposition from the British, as well as the local Chinese and other foreign shipping companies. The chairman of the commission, therefore, refused to sign the contract, and it was held in abeyance pending consideration by the Inspector-General of Customs and the Central Government. A new Commissioner of Customs (British) was appointed, who agreed with the views of the shipping companies, and their interests have since been strongly supported both by him and by His Majesty's consul. No definite decision had, however, been taken in regard to the validity or otherwise of the abortive contract, when at the end of November the Minister of Finance, in spite of the fact that two repayments of the loan of 1918 had already been made in accordance with the above-mentioned arrangement of 1932, and that the commission were carrying on negotiations for the improvement of the harbour, declared the 1932 arrangement cancelled and again demanded repayment of the loan in a lump sum.

Tariffs.

As the result of a sudden and unexpected decision of the Central Political Council, a revised Chinese import tariff was brought into force on the 22nd May, after the Minister of Finance had left for America and England. It was believed to have been drawn up largely by Dr. Soong's American advisers, against the advice of the Inspector-General of Customs and of the Chinese experts in tariff matters, who had not even been consulted. Certain of the enhanced rates were clearly levelled at Japan, the period of protection from higher rates, laid down in the Sino-Japanese Tariff Agreement of May 1930 to be in force for three years on certain classes of cotton goods, &c., having just expired. The new tariff greatly increased the rates on cotton, woollen, artificial silk, and other fibre manufactures, Chinese food-stuffs, and paper. The objects of the tariff may be said to have been (1) to secure an enhanced revenue as by striking a blow at Japanese trade; (3) to encourage local industry (particularly in the manufacture of cheap textiles); and (4) to establish higher tariff rates for bargaining purposes (especially at the then forthcoming World Conference). Unfortunately, the higher rates on certain cotton piece-goods ostensibly levelled at Japan were equally, and in some cases more, calculated to hit the trade in the higher grade United Kingdom textile products, the prices of which were likely to become prohibitive to all but the wealthiest classes. The new tariff made radical changes in the classification of both commodities and specific duties, making comparisons between the old and new rates difficult. It was feared that it might greatly reduce the trade in textiles as a whole from the United Kingdom, and that the volume of our trade in cotton piece-goods might even be halved, to the advantage of local production and of Japanese imports. A probable decrease in the import of certain commodities, coupled with an increase in smuggling, as well as of local production, rendered it unlikely that this higher tariff would result in any increase of revenue. Various objections to the rates of the new tariff were raised by the representatives of interested Powers. The French objected to the increase of the duties on anthracite coal, which they held to be contrary to their treaty with the Chinese Government (still awaiting signature)

concerning trade with Indo-China. The Japanese made representations, chiefly stressing discrimination against Japan, the failure to give any notice of enforcement, and the general ineptitude of such a policy at a moment of great delicacy in the relations between China and Japan, and on the eve of the World Economic Conference. The United States Government made no representations, as the principal imports from the United States of America were not affected. The question of the harmful effect on United Kingdom trade of many of the increased rates in the new tariff, particularly on cotton, artificial silk and woollen textiles, was taken up by the President of the Board of Trade informally with the Chinese Minister of Finance, who was then on a visit to England, and detailed criticisms were furnished to him. Dr. Soong was, however, unable to take any decisions in England, but promised full consideration of the position on his return to China, though he made it clear that such consideration would be all the more likely to be favourable if he obtained the export credits that he was seeking in England (see section on Finance and Taxation of this report). Dr. Soong deprecated the suggestion that any discussion should be opened, or representations made, regarding he new tariff pending his return to China, and it appeared doubtful to His Majesty's Minister whether any concrete results could be obtained in his absence, though it was, on the other hand, by no means certain whether on his return to China Dr. Soong would resume the same unique position of authority in the Government he had previously held.

267. The new duties also created difficulties for the Canadian trade in flour, and salt herrings and salmon, while they had a serious adverse effect on Hong Kong's local manufacturing as well as entrepôt trade. There was some difference of opinion between the Manchester and the Shanghai British Chambers of Commerce as to the maximum rates that various classes of cotton goods could bear in order to ensure the maintenance of an adequate export trade from the United Kingdom to China in these goods. The Shanghai Chamber feared that a demand for too great reductions might lead the Chinese to refuse to negotiate.

After his return to China in September Dr. Soong told the commercial counsellor that he intended to revise the tariff again in May 1934, but that he could not do so earlier owing to internal political difficulties, and to the fear that revision favourable to us would be considered as hostile by the Japanese. Meanwhile, he appointed a member of the Tariff Commission, Mr. Kan Lee, to discuss all items of interest to United Kingdom trade with Mr. Beale, but he insisted that such discussions must be kept strictly confidential, so that any subsequent revision should appear as a spontaneous act of the Chinese Government. Mr. Beale and Mr. Kan Lee had framed certain definite recommendations for the emendation of items in the tariff in which United Kingdom interests are predominant, when the Minister of Finance resigned at the end of October. It was understood at that time that the Japanese had been making informal, but definite, representations to the Nanking Government regarding revision, which Dr. Soong had been firmly resisting. The latter's resignation placed His Majesty's Minister in the difficult position of having to decide whether it would be better to continue to trust Dr. Soong, who might soon return to office, to steer these confidential negotiations through to a satisfactory issue, or to regularise the situation by a more formal approach to his successor or to the Government at Nanking. According to Dr. Soong the latter course would inevitably expose us to the risk of incurring odium for having linked ourselves up openly and officially with the Japanese on a matter on which Chinese opinion felt strongly. He said that nothing definite could be done in regard to changes in the tariff in any case till May of 1934, and it had been his intention to introduce the modifications we desired of his own accord. It was clearly impossible for the Nanking Government to agree to negotiate on tariff matters with His Majesty's Government in the United Kingdom while refusing to negotiate with Japan, and the only course open to us appeared to be to continue to trust to Dr. Soong's good offices, and not raise the question formally, unless and until negotiations were actually opened between China and Japan. His Majesty's Minister, nevertheless, just before his departure from China, made strong informal representations to General Chiang Kai-shek, Mr. Wang Ching-wei and Dr. Soong against the increased While not questioning China's right to raise her tariff he emphasised the adverse effect these duties were having on United Kingdom trade, with the

corresponding reaction on Anglo-Chinese relations. He also wrote personally to Dr. H. H. Kung expressing the hope that he would authorise the tariff experts of the Ministry of Finance to continue their discussions with Mr. Beale.

Manchukuo Tariffs.

ariffs of Manchukuo, to be preliminary to a fundamental revision extending over three years, was promulgated on the 22nd July, to take effect from the 23rd July. As regards the import tariff, the avowed objects of this revision were to lighten the burdens of the masses by lowering the duties on necessities, to encourage foreign trade by lowering rates savouring of discrimination or protection, and to develop domestic industries by cheapening the cost of machinery and equipment. The revised rates covered a comparatively small number of items; they were, in many cases, not more than half the former rates, which were the rates prevailing in the Chinese customs tariff prior to the revision of the 22nd May, 1933. While the new rates might be held to be generally more favourable to Japan than to other sources of supply, they foreshadowed improved opportunities for the United Kingdom in machinery, woollen piece-goods, and building materials, and to the United States of America and Canada in agricultural machinery.

Consular Invoices.

270. The regulations promulgated in 1932 (see section 215 of last year's report) have worked smoothly, and such objections as British exporters have raised on certain points involving unnecessary hardships have been met by the Chinese departments concerned on a spirit of conciliation and compromise.

VIII.—CONSERVANCY.

- (a) Haiho Conservancy.
- 271. The work of the Haiho Conservancy Commission, which is an international body charged with the maintenance and improvement of the Hai Ho from Tientsin to the sea, and of the Bar Channel, has become increasingly difficult during the past few years owing partly to natural causes, but more particularly to departmental squabbles and lack of co-operation on the part of the Chinese Government organisations concerned.
- 272. The main problem with which the conservancy is faced is the fact that practically the whole of the river system in Hopei drains into the Hai Ho, which, in time of flood, is quite incapable of carrying away the enormous mass of heavily silt-laden water which is poured into it, particularly from the Yung Ting-ho, which enters just above Tientsin.
- 273. Since 1931 seven different palliative schemes have been put forward, not one of which has it been possible to carry through owing principally to obstructive tactics on the part of landowners and the refusal of the provincial authorities to expropriate the land required. As a result the river was closed to navigation in 1932.
- 274. In 1933 the Improvement Commission did succeed in diverting the spring freshet, but within one month the position was completely changed. The summer freshet began very early, and when on the 12th June the engineer-inchief of the Hai Ho Conservancy warned the authorities that steps must be taken immediately to prevent the waters of the Yung Ting-ho from entering the Hai Ho, it was discovered that the chairman of the Provincial Government, unknown to the engineer-in-chief, but with the knowledge of his Chinese colleagues on the Improvement Commission, had promised the farmers in the settling basin area that no diversion would be allowed before the 22nd June. When at last action was taken on the 17th June, the harbour, from the point of view of navigation, had been completely ruined for the time being. Thanks to natural causes combined with dredging operations a certain amount of lost ground has been recovered, and in November coastal vessels were once more able to reach the Tientsin bund, but unless an effective plan can be put into operation without delay it is inevitable that a similar, if not greater, catastrophe will occur next year.

275. An eighth scheme has now been evolved, which would entail the expenditure of a further 2 million dollars. In the meantime, however, the Central authorities have decided that the Improvement Commission shall be closed down at the end of this year. According to an article in the Chinese press, the chairman of the Hopei Provincial Government is reported to have said that the uncompleted portion of the palliative scheme is to be carried on by the North China River Commission. The position is at the time of writing uncertain but all possible steps have been taken to bring home to the authorities concerned the gravity of the situation.

(b) Liao River Conservancy Board.

276. As a result of conservancy funds not even being on a maintenance footing, the Conservancy Board have been obliged to discontinue all dredging work during the year. In view of the consequent risk of the bar rapidly silting up, the Commissioner of Customs suggested to His Majesty's consul at Newchwang in September that His Majesty's Government in the United Kingdom should agree to the conservancy work being transferred from the board to the Manchukuo authorities. Enquiries from local British commercial interests showed that they would have no objection to such a transfer. In view, however, of the political complications which might follow on His Majesty's Government being involved with the Manchukuo authorities in the liquidation of the board set up in agreement with the Chinese Government, it was felt that while His Majesty's Government would not object if the board was in fact liquidated, it would be preferable not to be concerned in any way as a party to such action. His Majesty's consul was therefore instructed not to attend the meeting of the board which took place on the 12th December. At this meeting a resolution was unanimously passed that the board should be dissolved and the management of the conservancy handed over to the Manchukuo authorities.

IX.—BOXER INDEMNITY.

- 277. Mr. W. H. Donald resigned in the spring from the board of trustees, and in June the Chinese Government appointed Mr. W. S. King in his place. Mr. King is chairman of the China Association, and a member of the British Chamber of Commerce and the China Association Joint Committee.
- 278. On the 3rd July there was laid the foundation-stone of the new building to be erected in Nanking for the offices of the board of trustees. The proceedings were opened by Dr. Chu Chia-hua, the chairman of the board and Minister of Communications. Speeches were also made by the Minister for Foreign Affairs and Railways. His Majesty's Minister was represented by Mr. Ingram.
- 279. On the 13th February the Chinese Government requested as a measure of temporary relief the postponement for a further year of the payments of the British, American and Italian portions of the Boxer indemnity, which were due to be resumed on the 1st March. After consultation with the United States and Italian Governments, His Majesty's Government in the United Kingdom, in a note of the 12th April, stated that they regretted that they were unable to comply with this request, as they believed that a further moratorium would seriously prejudice the important purposes mutually beneficial to China and the United Kingdom, to which the funds in question were devoted. The United States and Italian Governments replied in a similar sense. Payments were not, however, resumed until the 31st May, when the instalment in respect of March was received. In spite of repeated representations, the instalments continued two months' in arrears until the end of October, when an order was issued by the Ministry of Finance to the Inspector-General of Customs for the payment in ten monthly instalments, beginning on the 31st October, of the two months' deferred instalments. In this way the indemnity service was to be brought up to date on the 31st July, 1934. The additional one-fifth instalment was duly paid on the date specified, and after consultation with the Americans, who had received similar payments, this arrangement was tacitly accepted. It is believed that the Italian instalments have continuously been paid for the last two years. and that, in their case, there has in practice been no moratorium.

- 280. On the 20th July the board of trustees signed an agreement with the Ministry of Railways to loan to them when required £4,700,000 for the completion of the Canton-Hankow Railway. This will, it is understood, include all materials purchased for the construction of the line through the London Purchasing Committee. As a result of informal discussions with Mr. Calder Marshall, the senior British member of the board of trustees, the Minister of tailways has given a definite assurance that all sleepers purchased out of this loan, which should be regarded as a loan secured on the funds themselves, will be obtained from either Canada or Australia.
- 281. On the 30th August a loan agreement was signed by the board of trustees, the Ministries of Communication and Finance, and the China Merchants' Steam Navigation Company, whereby the board has agreed to loan to the latter company a minimum of £360,000 and a maximum of £400,000 out of the accumulated indemnity funds appropriated to conservancy works apart from those funds for the Hwai River Conservancy Commission. The whole of the loan will be spent in Great Britain by the London Purchasing Committee. It is intended to build four steamers complete in Great Britain, and to purchase there the entire material for two steamers to be constructed in China.
- 282. The proceeds of the loans made by the board of trustees and available for educational purposes amounted at the beginning of September to over 400,000 dollars, and it is hoped that by the end of the year the sum available will be more than double this amount. No definite decision has yet been reached as to the disposal of these funds, but certain proposals are now under consideration. Nine Chinese students were awarded scholarships by the board of trustees, and sailed for Great Britain on the 5th September to pursue there advanced studies.
- 283. A Sino-British Cultural Association has recently been established in Nanking, and the inaugural meeting, which His Majesty's Minister attended, was held on the 11th October. The promoters of the association, which is of entirely spontaneous origin, include the Minister of Education, who is the chairman, and other prominent personages at Nanking. The association has set itself an ambitious programme, including the interchange of lecturers, the establishment of a library, the publication of pamphlets and documents, &c. In order to carry out these proposals, it is relying to a large extent upon the support which it hopes it will secure from the board of trustees.
- 284. An exchange of notes took place on the 14th April between the Dutch Minister and the Waichiaopu, whereby the Dutch Government remitted all payments on the Boxer indemnity as from the 1st January, 1926, to the Chinese Government. Of the sum remitted 65 per cent. is to be devoted to conservancy work in China, and the remaining 35 per cent. to cultural purposes. Of the former portion part is to be handed over to the Survey and Research Institute in Nanking, and the remainder is to be used for conservancy work in the same city. Just over one-half of the annual income from the cultural endowment fund is to be handed over each year to the Academia Sinica in China, who will use the greater part of it in the form of scholarships for Chinese students to be sent to the Netherlands. The remainder is to be donated each year to the Sinological Institute at the University of Leyden.

X.—AVIATION.

Appointment of Air Attaché.

285. In 1932 a proposal was put forward to His Majesty's Government by His Majesty's Legation for the appointment of an air attaché to China. It was thought that he would be able to co-ordinate the efforts of all British aviation interests in this country, thus enabling them better to compete with foreign aviation activities, and to further in this way the sale of British aircraft and material. At the end of July it was announced that His Majesty's Government had appointed Wing-Commander R. P. Willock to the post, and after full consideration it was decided that, in view of the importance of the maintenance of close contact with the Central and Southern Chinese aircraft markets, his headquarters should be at Shanghai. Wing-Commander Willock left for China before the end of the year.

British Aviation Mission to China.

286. Air Marshal Sir John Higgins, acting chairman of Armstrong Whitworth (Limited), and Messrs. A. V. Roe and Co., accompanied by Colonel Badham-Thornhill, D.S.O., reached China in April. The object of the mission was to get into touch with leading Chinese in the military and political spheres with a view to increasing the sale of British aviation material in China, and at the same time counteracting the activities of the United States Aviation Mission. The British mission, which was joined in Shanghai by Mr. Vaughan Fowler, managing director of the Far East Aviation Company, visited His Majesty's Minister in Peking and was given all facilities to meet Chinese Government officials. During their stay the mission was received by General Chiang Kai-shek and Dr. H. H. Kung, director of the Central Bank of China, to whom a detailed scheme for the organisation, training and equipment of the Chinese air force was submitted. The scheme provided for the supply of approximately seventy aeroplanes with staff at a cost of £500,000. It was found impossible, however, to reach agreement on terms of payment, and the mission left China in September.

Sale of British Aircraft.

287. Considerable sales have been effected by British aircraft representatives in various parts of China, particularly through the Far East Aviation Company, who have been most active with the assistance of demonstration machines in securing a large volume of business in spite of severe foreign competition. Although the high quality of British aircraft is generally admitted by the Chinese authorities, United Kingdom manufacturers have undoubtedly been placed at a distinct disadvantage vis-à-vis foreign interests in view of their inability to accept the credit terms offered by the Chinese Government without official financial backing and assistance which the Export Credit Guarantee Department is not prepared to give. It is agreed, therefore, that United Kingdom firms would be well advised to concentrate on securing smaller orders which they could finance themselves, and for which the Chinese could find adequate security

288. In January the commercial counsellor discussed with the Minister of Finance a scheme for a coast patrol air arm for the Chinese Maritime Customs Service, prepared by the Far East Aviation Company. The scheme involved the supply of seaplanes and the establishment of a seaplane school controlled by a British airman. The proposals were later discussed with the Inspector-General of Customs. Although large sums had been included in customs budget for contract, up till the end of the year no further progress has been reported.

289. For some time past the Chinese Government have been anxious to enlarge their military air force, and during the year efforts have been made to obtain orders from the Chinese authorities for British military aircraft. The only firms interested in these proposals have been (a) Messrs. Armstrong Whitworth Aircraft (Limited) and Messrs. A. V. Roe and Co., represented by the Far East Aviation Company; (b) Messrs. Hawker Engineering Company (Limited) and Messrs. Rolls Royce, represented by Messrs. Reiss, Massey and Co.; and (c) Messrs. Vickers (Aviation) (Limited) and Messrs. Bristol Aeroplane Company (Limited) represented by Messrs. Jardine Engineering Corporation (Limited). All these firms have submitted schemes of varying magnitude to Dr. H. H. Kung, who appears to be the chief Chinese official concerned with the purchases of aircraft. In the case of Messrs. Reiss Massey and Co.'s proposal to supply 190 machines and erect an aircraft factory, involving a cost of £2,300,000, the Chinese authorities were informed that if a contract were arranged the Air Ministry would be willing to grant flying and other training facilities to a number of Chinese officers. On the other hand, the offer of Messrs. Jardine Engineering Corporation (Limited) only provided for thirty aeroplanes at a cost of £320,000. In nearly every case the system of payment offered by the Chinese authorities, i.e., three- to five-year period with instalments guaranteed by the Central Bank of China, has been the principal obstacle for British interests.

Foreign Aviation Interests in China.

290. Although British aircraft manufacturers have succeeded in securing numerous orders, they are encountering more and more severe competition from American and Italian aviation interests. American interests are strongly represented in China, and are strengthened by the fact that the chief commercial aerial

services are in the hands of a Sino-American company (China National Aviation Corporation), employing none but American-made machines flown by United States pilots. In addition, Pan-American Airways has inaugurated an air-mail service between Shanghai and Canton. It stands to reason, therefore, that the predominant position of America in the commercial sphere, as well as the presence of the Hangchow flying school for the training of Chinese pilots, under American upervision, have meant that air-minded China thinks of military and commercial flying in the terms of American machines.

- 291. At the beginning of the year the Curtiss Aviation Company sent Major Doolittle to China to conduct an advertising campaign for their aircraft. He gave exhibition flights over Shanghai, and it is probable that his activities may have resulted in his securing contracts for his firm. The representatives of the Curtiss Wright Group and the Boeing Company have been most active in dealing with the Central and Provincial Governments, giving demonstrations and interesting China in aviation according to American ideas. It has been reliably reported that a scheme has been submitted to the Minister of Finance by the Curtiss Wright and Douglas Group for the erection, at their expense, in China of an aircraft factory capable of producing 600 aeroplanes per month. The construction of this factory is, it is understood, to be started on shortly, probably near Nanking.
- 292. Italian aviation interests are steadily gaining in importance in the hands of Colonel Lodi, Italian air attaché at Shanghai. It is believed that the Italian Government have offered to finance aircraft sales to the Chinese Government for long periods on easy terms, using in part the Italian remitted Boxer indemnity funds. In any case, Colonel Lodi appears to be empowered to negotiate contracts with the full support of the Italian Government. In June Dr. Kung informed the commercial counsellor that Italian interests had offered to supply up to 300 machines and erect a factory on a five-year plan, taking as security the guarantee of the Central Bank of China to make monthly payments.
- 293. Colonel Lodi arrived in China in October as administrative head of an Italian air mission, and will be joined later by Colonel Bernhardi, who will act as the technical head of the mission. It is believed that the mission may take over the training of the bombing section of the Chinese air force.
- 294. Neither French, German nor Japanese aviation interests are at present serious competitors, although it appears that the French have succeeded in placing a considerable number of small orders. German interests are principally confined to the Eurasia Corporation Commercial Air Service. As far as Japan is concerned, it appears that the military elements are much exercised at the present American predominance in air matters in China.

Air Routes.

295. From the British point of view, the chief interest has centred on the establishment of an air service between Shanghai and Canton, in view of the fact that the Far East Aviation Company had been endeavouring to obtain facilities, either independently or in co-operation with Imperial Airways, for the operation of the whole or part of the itinerary. Their chief rival has been Pan-American Airways, which recently bought up 45 per cent. of the interests of the China National Aviation Corporation, and immediately began to explore the possibility of establishing an air mail and passenger service between Shanghai and Canton, using Hong Kong as a port of call. At the same time Pacific-American Airways, a subsidiary company, was planning to operate a service from Manila to Hong Kong as a link in their Trans-Pacific Service. It was realised that the acquiescence of the Hong Kong authorities must be used as a lever in any representations either to Pan-American Airways or the Chinese Government on behalf of the Far East Aviation Company, who had already at the end of 1932 been refused facilities to establish an air-mail service between Hong Kong and Hanoi. Although discussions took place between the commercial counsellor and the representative in Shanghai of Pan-American Airways as to the possibility of the latter's co-operation in securing facilities from the Chinese Government for a British company to operate a service between Shanghai and Canton, it was not

found possible to find a satisfactory basis of agreement. On the 24th October Pan-American Airways inaugurated a bi-weekly service between Shanghai and Canton without including Hong Kong in the itinerary.

296. Other air routes in operation are those operated by the China National Aviation Corporation from Shanghai to Peking via Tsingtao and Tientsin and from Shanghai up the Yangtze River via Nanking and Hankow to Chungking The Eurasia Aviation Corporation have been running a service linking up Nanking and Peking via Loyang and Sianfu with the Provinces of Kansu and Sinkiang, as far as the Soviet border when conditions permit. They have also taken steps to inaugurate a service between Hankow and Canton, but so far only trial flights have taken place. It is understood that the Eurasia Aviation Corporation have an extensive programme of expansion under consideration.

XI.—LEGISLATION.

- 297. The subject of legislation during 1933 lends itself to consideration under two different headings, namely, (a) new legislation, and (b) enforcement, or attempted enforcement, of existing legislation, the latter assuming particular importance on account of the resultant effects on British interests.
- 298. As the outcome of certain local developments, the Chinese authorities revived their pretensions to the control over factory inspection in the Shanghai International Settlement on the strength of the series of factory and factory inspection legislation issued during 1929–31. The Chinese authorities similarly pressed for compliance on the part of British interests with the registration requirements of the various company and press (or publication) enactments of 1928–31, as well as continuing to maintain that British shipping in Chinese waters should submit to the control of the navigation bureaux in the exercise of the functions prescribed by the Shipping Law of 1930 and various supplementary legislation. In all these cases the views of His Majesty's Legation on the subject, representing a reasonable compromise to the mutual benefit of all parties, have so far failed to elicit a reciprocal response, and a definite solution is accordingly still pending.
- 299. With regard to new legislation, the following measures, also incidentally connected with shipping, may eventually prove in some way or other to conflict with British navigational and other treaty rights, and are therefore of particular significance: The Provisional Yangtze Regulations of 1933, declared by Customs notification to supersede the Yangtze Regulations of 1898 as from the 15th May; the Regulations for the Control of Towed Vessels, the date of actual operation of which, originally fixed to coincide with the date of promulgation, the 5th June, was subsequently postponed till the 1st December; and the Commercial Ports Ordinance of the 27th June, the date of enforcement of which is still pending, designed to introduce a more uniform system of harbour regulations for the whole of China. Although under existing conditions they do not primarily affect other than vessels under Chinese jurisdiction and their personnel, mention should also be made of the regulations of the 28th April conferring authority on the various navigation bureaux to set up Shipping Collision Disputes Settlement (or Arbitration) Committees, and the mandate of the 18th May and subsequent detailed enforcement rules whereby the Ships' Officers' Test Legislation referred to in paragraph 246 of last year's annual report was rendered operative as from the 1st June.
- 300. To the predominating influence of two phases of the general situation in China can be ascribed the origins of a considerable proportion of the year's legislative production, namely, the interest in military matters inevitably aroused by the lessons of the anti-Japanese and anti-Communist campaigns, and the acuteness of the economic crisis. The measures initiated with the object of restoring prosperity, particularly in the rural districts, where conditions were aggravated by natural calamities and brigand ravages, were recently enumerated in Sir Miles Lampson's despatch No. 1448 of the 7th November, and do not, therefore, require detailed recapitulation. It will be sufficient to recall that they embraced a wide range of subjects, such as forestry, fishery, waste-land reclamation, water conservancy, development of native products and industries, and

large-scale rural rehabilitation, and that their operation was to be facilitated and centralised by the provision of a Rural Rehabilitation Committee under the regulations of the 19th May, as amended eleven days later, and the enlargement and reconstitution of the National Economic Council of 1931 by a new organic law of the 23rd September. The following financial measures should also be recorded as contributing to the general scheme of economic reorganisation: the Silver Standard Unit Minting Ordinance of the 8th March, regulating the official monetary system following the abolition of the tael as a current unit; the regulations adopted by the Central Political Council on the 11th June for the institution of a State lottery to raise funds for aviation and highway development; and two Acts defining the principles for the compilation of local budgets and the limits of the authority of local Governments in matters of financial administration.

- The "military-mindedness" of present-day Chinese legislators was already indicated by the series of ordinances, &c., dealing with military routine and reorganisation enumerated in paragraph 248 of the previous annual report. A number of similar enactments were successively issued during the course of the present year also, of which the most notable was the Military Service Law promulgated on the 17th June, but not yet enforced, in supplementation of the "principles" adopted the year before. The safe-guarding of confidential military information, already partially provided for by the Strategic and Fortified Zone Law of 1931, was further ensured by a Military Secrets Protection Law, which, though actually promulgated on the 17th December, 1932, remained for a while in abeyance, being eventually put into force for a period of nine months, commencing from the 1st April by a mandate of the 22nd March. Restrictions on the taking of cinematograph pictures by foreigners in Chinese territory and the subsequent removal abroad of the films were probably also partly framed in the interests of military secrecy. These were contained in certain special rules issued on the 22nd May and in an amendment on the 15th August of articles 8 and 9 of the Cinematograph Censorship Law Enforcement Rules of 1931. The control of map compilation was further regulated by the promulgation on the 21st September of detailed enforcement rules for the 1931 Ordinance for the Examination of Maps and Hydrographic Charts, while the requisitioning of maps by the military were regularised by special provisional rules issued on the 7th October. The uninterrupted production of military material was probably the motive of an amendment of the 20th June to article 3 of the 1929 Labour Union Law, whereby all classes of employees, whether clerical or manual, of organs connected with military affairs or industries were specifically excluded from the right of forming labour unions.
- 302. The organic law of the National Government escaped its almost annual revision, but minor amendments were incorporated in the constitutional legislation of its subordinate Control, Examination and Legislative Yuans, as well as of the Ministries of Communications, Education, Audit, and Official Ranking, while the creation of a special new Ministry to deal with frontier affairs was also mooted. At the same time a preliminary draft of a final Constitution for China, prepared by an ad hoc committee, was published during the course of the summer for general criticism. Other constitutional legislation includes the ordinance governing the offices of Cultural Commissioners for the Mongolian Banners and Western Borders respectively, and the enforcement mandate of the 11th March of the municipal and district councils organic and election laws. This was followed on the 6th July by rules defining the procedure for municipal council meetings.
- 303. An ordinance prescribing the date upon which new legislation should be considered as operative in the various regions of China, which was issued on the 23rd December, 1932, was not recorded in time for inclusion in the previous report. This and a revised version of a general outline of legislative procedure constitute the most noteworthy measures dealing with purely legislative routine.
- 304. The particular aspects of Chinese judicial methods most criticised by foreign residents were progressively studied by Chinese legal experts, assisted by Dr. Georges Padoux, French adviser to the Chinese Government on judicial matters. The immediate result of their labours was the issue on the 22nd May and the 15th June, respectively, of two ad interim instructional measures entitled "Supplementary Regulations (or Instructions) relating to Execution in Civil Cases" and "Points of Procedure to be observed in dealing with Civil Cases."

At the same time various orders forbidding the denial of bail without due justification and the use of torture for the extraction of evidence, &c., doubtless designed to impress the public rather than with any expectations of their being honoured by the recipients, were successively issued by the Ministry of Justice, who were also responsible for an announcement of the pending revision of the Civil and Criminal Codes and the Code of Civil Procedure. Other important judicial measures were the enforcement mandate of the 22nd June of the 1932 Administrative Actions Law; the Supreme Court Revised Organic Law on the 14th August; and the Police Weapons (use of) Ordinance of the 25th September. The Prize Court and Maritime Prize Ordinances, promulgated on the 15th December, 1932, having been made public too late for inclusion in that year's report, are accordingly also here recorded.

305. More than twenty separate measures dealing with civil service examinations of all classes have been listed during the year under review. The number of regulations and bye-laws relating to the conduct and curriculum of universities and primary, middle, normal and vocational schools, as well as other scholastic subjects is scarcely less.

XII.—PROPAGANDA.

306. The dissemination of official news and propaganda is mainly under the control of the Central Publicity Committee of the Kuomintang, which works under the Central Executive Committee of the National Government. The Publicity Committee is responsible for propaganda both in China and abroad. It controls the Central News Agency, which now has its own wireless stations at Nanking, Shanghai, Peking, Tientsin, Hankow, Loyang and Sian. It is also through an "Arts Department" responsible for all picture-posters, news-reels and pamphlets, and controls, it is understood, the censorship of films. The Publicity and Intelligence Department of the Waichiaopu also takes its orders from the Publicity Committee. The former's activities are no longer limited to collecting information on current events and preparing documents, but approximate to those of the News Department of the Foreign Office.

307. The Kuomin News Agency is now almost entirely a private concern, which is under the control of the Publicity Committee of the Waichiaopu, and is subsidised by them to the amount of from 5,000 to 12,000 dollars a month.

308. At the time of the Japanese drive towards Peking, there was temporarily created a super authority, to decide the press policy of the Government, under the name of the Public Opinion Control Committee. During that period no news could be published without the consent of one of its three members.

309. New wireless receiving and transmitting sets are being installed at the Chinese Government Radio Station at Chenju, providing for a beam wireless service with England and America, and direct communication with those countries by wireless, telephone or telegraph. Additional aerial towers are being erected at Chenju and Liuchiaching. The new installation, which should operate early in the new year, will not transmit or receive broadcasts which will be provided for independently. The Central Broadcasting Station at Nanking, which is controlled by the Central Party Headquarters, daily broadcasts news and propaganda.

310. The activities of the French News Agency Havas have been considerably extended in China. They have developed their service to cover news of special interest to China, and owing to the large volume of material which their association with the French Government enables them to carry, they have frequently overshadowed Reuter's news service in the press. At the end of 1932 Havas attempted, without success, to obtain subscriptions from Shanghai newspapers, and the service is therefore still issued free of charge. They succeeded, however, in securing small contributions from the Chinese press, who now publish the Havas service more prominently than formerly.

311. Outside Shanghai, Havas, whose articles are often anti-British in tone, have been concentrating on breaking down the leading position still enjoyed by Reuter's as an agency for distributing foreign news to the vernacular press in

China. In Peking and Tientsin the large volume of news distributed by Havas through the French official wireless stations, with the support of the French Government, has seriously affected the position of Reuter's. In Nanking, where Reuter's have a virtual monopoly of foreign news published in the Chinese newspapers in virtue of an agreement with the Chinese "Central News Agency," to whom Reuter's have handed over the release of their despatches to the press, was have made inroads, and it is understood that representations have been made by the French Minister to the Chinese Government on behalf of the French publicity service. It is also reported that Havas are conducting negotiations with a view to distributing a foreign news service in Manchukuo, on the understanding that both inward and outward news is subject to Japanese control.

- 312. As much assistance as possible has been given to Reuter's by His Majesty's Legation, with a view to meeting increased competition. Arrangements were made at the beginning of the year whereby the British official wireless is made promptly and readily available to Reuter's agents in Hankow, Nanking and Canton by His Majesty's ships and consular officers. Separate arrangements are in force in Shanghai, whilst Peking and Tientsin are served by His Majesty's Legation wireless station, although the service has for technical reasons been somewhat irregular.
- 313. Both the United Press and Associated Press of America are also extending their influence in China. The former, although receiving no direct assistance from the United States Government, obtains support from American business interests in Shanghai. The Associated Press, moreover, have made efforts to undermine the position of Reuter's in Japan by breaking down their arrangement with Rengo, with the idea later of establishing a large news service in China, but it is believed that this machination has so far been foiled by Reuter's.
- 314. In February considerable prominence was given in press messages from England to the anti-Chinese and pro-Japanese tone of certain organs of the press in England on the proceedings at Geneva. An anti-British agitation soon flared up in the press, and news agencies and anti-British articles were regularly making their appearance in the Chinese newspapers of Shanghai, Nanking and other centres. The general tendency of the editorials was to attribute the failure of the League to give China satisfaction to the machinations of His Majesty's Government in the United Kingdom, who were suspected of abetting the aggressive designs of Japan as the result of some secret understanding with the Japanese Government in return for a free hand in Tibet and other concessions. The whole question was taken up by His Majesty's Minister with the Minister for Foreign Affairs, who was inclined to believe that the rumours were started by the Japanese to divert part of the odium of the Chinese public from themselves to Great Britain. The press campaign was in no way diminished by the activities of the Havas and Tass Agencies. The agitation quickly died down.
- 315. There was a private exhibition in Peking at the beginning of December of the Nazi propaganda film—"Deutschland Erwacht." Invitations to attend the performance were sent out by the German Minister, and the audience included prominent Chinese officials, members of the Diplomatic Corps and Chinese returned students from Germany. The film was also shown privately in Hankow and Nanking.
- 316. His Majesty's consul-general at Mukden reports that propaganda activities in Manchuria have been undertaken exclusively by the Japanese. The Bureau of Information and Publicity of the Department for Foreign Affairs at Hsinking, which issues periodically official bulletins in English, is directed by a Japanese official, who is undoubtedly the fountain head of all propaganda in the country. The Manchukuo News Agency, which issues daily bulletins in Japanese, Chinese, and English, was announced, at the time of its inception, as having taken over the work of both the Rengo and Nippon Dempo News Agencies throughout Manchuria. It has its head office at Hsinking with branch offices in the more important towns. The agency also broadcasts news, &c., daily from Hsinking by radio. There is a vice-consul attached to the foreign affairs section of the Japanese consulate-general at Mukden, who meets foreign correspondents in the

consulate twice a week, and replies to questions which they have submitted in advance.

The question of the registration of foreign-owned publications in China under article 7 of Law of Publications and its Detailed Enforcement Rules has been the subject of continual negotiations during the year. In May the Waichiaopu addressed a note to His Majesty's Legation, requesting that the head offices of newspapers and periodicals issued in China by British nationals should be a continuation of the cont In May the comply with the requirement for registration with the Ministry of Interior. As it was at the same time made clear that the Chinese Government had authorised the suspension of the enforcement of registration with the Central Party Headquarters and of the penal clauses, and that foreign newspapers having registered with the Ministry of Interior would become automatically entitled to receive the protection of the Chinese Government and enjoy reduced postal facilities, His Majesty's Legation, in agreement with the United States Legation, replied that, provided that the requirements of registration were, in practice, found to be in consonance with the assurances given, they would be prepared to advise the British interests concerned that there was no objection to registration. Since then the Waichiaopu have twice endeavoured to discuss the attitude of His Majesty's Legation, and to explain the difficulties with which the Chinese Government were faced, but the line taken by His Majesty's Legation has been that, if the question is to be pursued, the forms of registration, &c., must first be submitted for inspection. The Waichiaopu accordingly at the beginning of December sent the Legation copies of the forms, which appeared generally satisfactory, and the question has now been referred to the Foreign Office for instructions.

XIII.—CLAIMS.

318. During the course of the year the Legation went again in detail into the question of what action should be taken regarding the checking and settlement of the lists of accumulated claims in the Legation archives, some of which had been outstanding for more than fifteen years. After careful consideration it was decided that there were two main alternative courses, of which the latter seemed preferable, either (1) to proceed by detailed scrutiny of the Legation files as well as by confirmatory reference to the claimants and His Majesty's consular officers at the ports concerned to check and reassess our claims, cutting them down so as to conform with the accepted standards of international law; or (2) to postpone such action until we had first discussed the matter with the Chinese Government and sought to come to some acceptable agreement with them upon the general principles which should govern the formulation of our claims. The question of which alternative should be adopted was referred to the Foreign Office for a decision, which, up to the time of writing, has not been received.

319. While the general subject of claims is, therefore, still under review, it has been possible this year, through continued representations to the Chinese authorities, to have the following individual debts and claims liquidated.

(a) Sums due in respect of arrears of salary, &c., due to the British ex-employees of the Tientsin-Pukow and Canton-Hankow Railways, amounting to 9,941.97 dollars, plus £2,845 17s. 3d. sterling, and 50,301.9 dollars respectively.

(b) A sum of 28,350 · 26 dollars due to Messrs. J. Whittall and Co. (Limited) in respect of materials supplied for the so-called Yamen Bridge

constructed between the years 1923 and 1926.

(c) Mr. G. E. Bell's claim for the loss of his property and effects at Pakhoi in December 1925, for which he accepted 14,000 Canton dollars in full settlement from the Kwangtung Provincial Government.

- 320. In addition, the following debts and claims have come a stage nearer final liquidation:—
 - (a) In respect of the amounts due to British creditors of Chinese railways for materials supplied, an agreement covering the Tientsin-Pukow Railway debts was signed on the 15th February by the Minister of Railways and Mr. R. Calder Marshall. Under this agreement the

principal of the total indebtedness was fixed at £149,125 14s. 2d. and 8,085,193·77 silver dollars, and it was provided that simple interest at the rate of 5 per cent. per annum should be charged on outstanding balances of this principal remaining unpaid. It was further provided that from the 1st January, 1933, until the principle and interest had been liquidated, the Ministry of Railways should, on the last day of each month, pay a sum of not less than 50,000 dollars. These monthly payments have, however, already fallen three months into arrears, but the Chinese Government, in a note of the 15th November, undertook that these arrears would be wiped off and that no further unpunctuality would be permitted.

(b) In respect of the amounts due for arrears of salary, &c., to British ex-employees of the China Merchants' Steam Navigation Company, an agreement was reached in March between the accredited representatives of the Officers' and Engineers' Guilds and of the company. Payments are to be made by the company in quarterly instalments spread over a period of five years, the first payment being made in

April of this year.

(c) In respect of the Nanking claims the Chinese Government paid further instalments amounting to 742,551 81 dollars. The payment of the last of these instalments in July was accompanied by a statement of accounts showing that up to that date 2,542,551.81 dollars had been paid, i.e., 2,317,689·14 dollars in respect of the claims for that amount assessed in Chinese dollars, and 224,862.67 dollars in respect of the sterling claims amounting to £20,917 9s. 13d. converted into dollars at the rate of 10.75 dollars = £1. The Chinese Government accordingly claimed that they had finally liquidated these claims. In practice, however, it had not proved possible to convert dollars into sterling at the rate of 10.75 dollars=£1 to meet the sterling claims, and our accounts were, therefore, still 110,640.47 dollars short. Moreover, it did not appear that the Chinese Government had any justification for laying down that the sterling claims should be converted at that or any other fixed rate. They were accordingly informed that we were unable to accept their statement of accounts as correct, nor to admit that the navments in question had been liquidated. In the meantime, the question of the line to be taken with the Chinese Government was referred to the Foreign Office for instructions.

321. Progress has also been made towards the settlement of the two categories of claims arising out of Sino-Japanese hostilities in Manchuria, noted in paragraphs 262 of the annual report for 1932: (a) Arrangements were made for the liquidation of the claims of foreign firms for payment of materials, &c., supplied to the former Manchurian authorities (see section on Manchuria); (b) an ex gratia payment amounting to 680·23 dollars has been made by the Japanese military authorities for damage to property by bombing. Other losses, however, through commandeering of stocks, &c., remain outstanding. In addition, the list of claims for losses at Shanghai prepared by His Majesty's consulate-general at that port were duly presented to the Chinese and Japanese Governments respectively on the 10th January. On the 3rd March the Chinese Government replied denying their liability for any of the claims presented, and it was decided that for the present no useful purpose would be achieved by returning to the charge against the Chinese Government. On the 24th June the Japanese Government addressed a note to His Majesty's Ambassador at Tokyo, also refusing to accept liability, but stating that as an exceptional measure of beneficence they were prepared to give favourable consideration under an Imperial Ordinance, allotting 3 million yen for the relief of those who suffered loss through the Manchurian incident, to a "very small number of" claims made by foreign nationals at Shanghai after a thorough investigation by the Japanese consulgeneral at that port. The acting British consul-general at Shanghai was accordingly instructed to get into touch with his Japanese colleague, and to furnish him with any information he might require.

Register No.

P. Z.

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POLITICAL DEPARTMENT.

Minute Paper.

Dated

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CHINA.

Annual Report, 1932.

[F 1562/1562/10]

Mr. Ingram to Sir John Simon.—(Received March 7.)

(No. 55.) Sir,

Peking, January 11, 1933.

I HAVE the honour to transmit to you herewith the annual report on China for the year 1932. I am indebted for this work to the members of my staff for their respective sections. Mr. Harcourt-Smith has been of great assistance in the general preparation and compilation of the report.

I have, &c.

E. M. B. INGRAM.

Enclosure.

Annual Report on China for 1932.

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I.—INTERNAL POLITICAL SITUATION.

(1) General.

THE year 1932 opened with a coalition Nanking-Canton Government in the saddle. The new Government included Lin Sen as President, Sun Fo as chairman of the Executive Yuan, C. C. Wu as chairman of the Judicial Yuan, and Euge Chen as Minister for Foreign Affairs. The other posts in the Government we divided up among the various factions of the Kuomintang. The Standing Committee of the Central Political Council—the highest organ in the State—was confined to three names, Chiang Kai-shek, Wang Ching-wei and Hu Han-min, the three great rivals who, ever since the death of their master Sun Yat-sen, had contended for political leadership. On paper the reunification of the party was complete, but in actual fact only nine out of the thirty-six members of the Government Council were in Nanking when the new régime was inaugurated on the 1st January, while all three of the members of the Standing Committee above mentioned remained in retirement. Chiang Kai-shek, having emptied the Treasury and established his military supporters in key positions in and around Nanking, had withdrawn to Chekiang; Hu Han-min, pleading sickness, was refusing to have anything to do with the new régime; Wang Ching-wei, who was really ill, remained at Shanghai awaiting developments. In the South the Kwangtung militarists, no longer interested in the fate of Sun Fo and his fellow politicians who had left Canton to join the Nanking Government, were concerned only with the retention of their own power. In the North Chang Hsueh-liang, in military control of all the northern provinces with the exception of Shantung and Shansi, was adopting an attitude of watchful waiting, loyal to the Central Government so long as it did what he conceived to be its duty.

- 2. As the Shanghai situation grew critical in the course of January the question of what attitude was to be adopted towards Japan was hotly debated. Sun Fo, Eugene Chen and the rest of the Cantonese group were, in general, strongly in favour of severing diplomatic relations, while the other members of the Government were equally strongly opposed to such a course and counselled a policy of conciliation at almost any price. At this moment Chiang Kai-shek and Wang Ching-wei allowed themselves to be persuaded to return to Nanking. Chiang, with characteristic energy, threw himself into the fray. He had all along been an advocate of conciliation and a passive policy as the less disastrous of the two roads open to the Government, and, following his lead, the Central Political Council on the 24th January voted for the acceptance of the Japanese demands with regard to Shanghai. Sun Fo and Eugene Chen promptly withdrew. Wang Ching-wei only remained, as he explained, out of a sense of duty, but declared his intention of retiring as soon as the crisis was past.
- 3. The Administration was now at one of the most critical junctures in the history of modern China, without an Executive Head of the Government, a Minister for Foreign Affairs or a Minister of Finance. The disorganisation of the Government and the nervousness of all its members was such that it seemed as though any serious collision at Shanghai was bound to result in the disappearance of all semblance of ordered government. However, frantic efforts were made to fill the vacant posts, and on the very day, the 28th January, on which the Japanese ultimatum was due to expire, Wang Ching-wei was induced to accept the post of president of the Executive Yuan and Lo Wen-kan that of Minister for Foreign Affairs. On the following day T. V. Soong was re-elected Minister of Finance, while military affairs were put in the hands of a committee, on which the leading militarists, headed by Chiang Kai-shek, all had places.
- 4. Hostilities broke out in Shanghai in the night of the 28th January. In the general uncertainty as to the ultimate objects of the Japanese it seemed possible that they might occupy Nanking. The main archives of the Government and the majority of the heads of Department were hastily transferred to Loyang, which was declared to be the temporary capital, but during the following days, as the impossibility of transacting urgent business from Loyang became apparent, the Ministers drifted back either to Nanking or to Shanghai.
- 5. On the 1st March the second plenary session of the Central Executive Committee was held at Loyang to discuss the political and military situation of

the Government and its future plans in reference to the conflict with Japan. The proceedings were not made public, but it was reported that the alleged failure of the Government to suport the XIXth Route Army, which had borne the brunt of the Japanese attack at Shanghai, and its consequent withdrawal were the subject of very severe criticism and heated argument. One interesting decision, which was made public, was that the chairman of the Military Committee (the existence which was now regularised) should be concurrently Commander-in-chief of the ational armed forces, and that Chiang Kai-shek should be the chairman of that committee. The astute Chiang had thus, as usual, turned the edge of his enemies' weapons and strengthened his position by the very measures designed by his political opponents to weaken it. The Organic Law of the Government had until December 1931 provided that the President (at that time Chiang Kai-shek) should be concurrently Commander-in-chief of the armed forces. With the special object of putting an end to Chiang's dictatorship the first plenary session of the Central Executive Committee had in that month amended the Organic Law so that the President became only the titular head of the State, the control of the fighting forces being removed from him. Chiang resigned, after having placed his own nominees in all the important military positions around Nanking and made it practically impossible for anyone to step into his shoes. The establishment of the Military Committee referred to in paragraph 3 gave him his opening, and, having arranged for his own appointment as chairman of that committee and concurrently Commander-in-chief, he was back at the point where he had been three months before except for the now empty title of President, which he was probably content to leave to another.

- 6. While Chiang was thus busy in restoring his personal ascendancy in the Government the Sino-Japanese armistice negotiations had been going forward at Shanghai, and the Armistice Agreement was signed on the 5th May. The signature of this agreement presented the Government with some hours of anxiety while the reaction of the country was awaited. On the whole, the Government was entitled to congratulate itself on the result, for almost unanimously the agreement was accepted, not indeed without criticism, but as possibly the best which could be obtained in the circumstances. Followed as it was by an immediate withdrawal of the Japanese forces, it had on the whole the effect of enhancing the prestige and strengthening the position of the Nanking group.
- 7. Freed from its immediate preoccupation with Japan, the Central Government once again turned its attention to the equally pressing menace of communism and banditry, the burden of which on the country had become well-nigh intolerable. General Chiang Kai-shek was put in charge of the anti-Red campaign, and in the early summer took up his headquarters at Hankow, from which point he has been directing a large-scale and, it would appear, effective offensive against the Communist and bandit hordes infesting the central provinces.
- Meanwhile the situation in the South had been developing. On the establishment of the unified Government in Nanking on the 1st January the so-called "National Government" at Canton had been dissolved. But it was too much to expect that Canton would surrender its individuality completely to Nanking, and it insisted on maintaining a branch Political Council (the "South-West Political Council") as a strong hint to Nanking that Canton would be quite ready to declare its independence again should its wishes be disregarded. The outstanding figure in South China was now Marshal Ch'en Chi-t'ang, a militarist who had no use for politicians and entangling alliances. Having got rid of the political incubus with the dissolution of the Canton "National Government" and the departure of Sun Fo and his clique to Nanking, Marshal Ch'en fixed his eyes on the pressing problems of coping with communism and banditry at home and consolidating his position, and left Nanking to deal with its own difficulties, international as well as domestic, as best it could. Beyond the despatch to Nanking of a squadron of six aeroplanes and the remittance of a considerable sum of money for the "comfort" of the XIXth Route Army, little was done by the south-western provinces to assist in the struggle against Japan, while locally every effort was made to avoid incidents which might lead to the extension southwards of the area of hostilities. When Sun Fo and the other dissatisfied politicians who had broken with Nanking [8425]

returned to the South and attempted to work up feeling against Chiang Kai-shek on account of his alleged failure to support the XIXth Route Army at Shanghai, they were very coldly received, not because Marshal Ch'en had any love for Chiang Kai-shek, but because he had his own axe to grind.

- 9. The relations between Canton and Nanking have always been in a state of flux, the particular degree of cordiality at any moment being usually dependent upon the regularity with which subsidies—or blackmail—are paid by the latte to the former. One outcome of the Japanese invasion of Shanghai was the suspension of the subsidies and a consequent cooling of the relations between Marshal Ch'en and Nanking. Marshal Ch'en accordingly proceeded to look after his own interests. There had for some time been friction between him and the Canton navy and air force (under Admiral Ch'en Chak and General Chang Hui-chang respectively). The causes are not very clear and in any case unimportant. At all events, Marshal Ch'en seemed to regard them as dangerous rivals to himself, and accordingly proceeded to bring them under his own control, though for the sake of appearances he purported to be acting at the behest of the South-West Political Council, whose value as a political puppet was thus demonstrated. On the 1st May the Chinese press announced the issue of a mandate by this council ordering the abolition of the Canton air force as an independent unit and placing it under the direct control of the Ist Group Army (i.e., Marshal Ch'en). On the 3rd May a second mandate appeared ordering the abolition of Naval Headquarters and placing the Canton navy under the personal control of Marshal Ch'en. The latter's intention was, it seems, to seize and disarm the navy at Whampoa, but, if so, the coup was only partially successful, for several of the bigger gunboats got away. They fled first to Hoihow and Chungshan, but, being harassed by attacks from the air, took refuge in Hong Kong harbour, where they were the source of much embarrassment.
- 10. The Hong Kong Government, in the first instance, gave notice that unless the gunboats left within twenty-four hours they would be interned. Only one of them left within the time limit, and the rest were immobilised by the removal of portions of their machinery. The Hong Kong Government were anxious not to become embroiled in a Chinese faction fight, and it was decided that the Central Government should be asked to say how the vessels were to be disposed of. Somewhat unexpectedly the Central Government replied requesting that the vessels be handed over to them. This was an awkward development, as the Canton Government were on their side claiming the vessels, and were threatening that their delivery to the Central Government would be regarded as an unfriendly act by Canton. While discussions were in progress the hostilities between Marshal Ch'en Chi-t'ang and Admiral Ch'en Chak came to an end, and so the occasion was taken to inform both sides—Nanking and Canton—that, since hostilities had ceased, the reason for the immobilisation of the gunboats no longer obtained and they were free to leave the Colony, the question of ownership thus being left to the two Chinese claimants to settle as best they could. When the Central Government found that the Hong Kong authorities had no intention of modifying their attitude, they soon came to terms with Canton, and the gunboats eventually left for that place on the 9th August.
- 11. As mentioned above, the hostilities between Marshal Ch'en Chi-t'ang and Admiral Ch'en Chak had meantime come to an end. General Ts'ai T'ing-k'ai and his famous XIXth Route Army were at this time being transferred from the Yangtze to Fukien to take part in the anti-Red campaign. General Ts'ai, himself a Cantonese and covered with glory as a result of his army's recent exploits at Shanghai, was invoked as an intermediary, and through his efforts a typically oriental settlement was effected, whereby Admiral Ch'en Chak's forces were to be incorporated in the XIXth Route Army for service against the Communists, and were to receive a monthly subsidy of 100,000 dollars for three months from Canton, while Hainan Island, which had maintained a practically independent status as the headquarters of the Canton navy, was to revert to the Provincial Administration. The relations of the two disputants with the Nanking Government during all this episode were bewildering in the extreme and perhaps not worth the trouble of disentangling. It seems to emerge, however, that Admiral Ch'en Chak, in refusing to surrender his fleet to the control of the Canton military junta, was fighting the battle of the Central

Government, and that, had conditions been different, the latter would have seized the occasion to reduce the growing pretensions of Marshal Ch'en Chi-t'ang. As it was, however, Nanking made the best of a bad business, and proclaimed to the world that, having abjured civil war as a political weapon, it was on principle not taking sides in the Canton dispute. The future policy of the Government, it was announced, would be, not to deal with recalcitrant provinces by force of arms, but to direct its attention to the consolidation of its position, politically and conomically, on the Lower Yangtze.

- 12. Meantime affairs in Nanking had not been going too well. Sharp divisions of opinion had developed among the members of the Government on three pressing problems: finance, the policy to be adopted with regard to Manchuria and the proposed resumption of Sino-Soviet diplomatic relations. By the middle of June all these questions were hanging fire and calling urgently for solution, but no final decision could be taken because General Chiang Kai-shek obstinately refused to return to Nanking to discuss them. As he would not come to the Government, the Government went to him, and a conference took place at Kuling in the middle of the month, when these important problems were threshed out. The financial situation was, indeed, desperate, and had recently been rendered even more acute by a combination of factors—the total cessation of revenue from all sources in Manchuria, a heavy fall in the revenues received from the provinces and the Shanghai customs and a rapidly increasing adverse trade balance. Suggested remedies varied from the declaration of a moratorium on all internal bonds and loan issues to a Government monopoly on opium. The conference, however, came to no spectacular decisions, but adopted proposals for a rigid scheme of retrenchment and the increase of certain customs duties. With regard to the other questions, it is believed that the resumption of diplomatic relations with Russia was approved in principle, and that, in view of the Government's financial straits and the unsettled internal conditions, any positive policy for the recovery of Manchuria was held to be out of the question.
- 13. During the last days of June it began to be rumoured that the Japanese, who had for some time been wooing General T'ang Yu-lin, the semi-independent Governor of Jehol, had become convinced of his "insincerity," and were preparing to invade the province, and it was even thought that, instead of doing so from the east, a difficult and dangerous task, they might come south of the Wall, and, by occupying Peking and Tientsin, cut off Jehol from the south. On the 17th July a Japanese liaison officer named Ishimoto disappeared on the Jehol-Manchurian frontier, and the Japanese, alleging—probably with truth—that he had been kidnapped by Chinese, sent a small armed force a short distance over the border to endeavour to rescue him. The expedition was unsuccessful, and the force was withdrawn after a skirmish with the Jehol troops. These events, which appeared to be the prelude to the expected invasion of Jehol, caused great excitement in North China. Marshal Chang Hsueh-liang telegraphed to General T'ang Yu-lin ordering him to resist to the last man, and made a pretence of sending forces to his assistance; but, in face of an announcement by the Japanese that any attempt on the part of Chang Hsuehliang to reinforce Jehol would entail serious consequences, his forces did not actually cross the frontier into that province.
- 14. When the news of the Japanese advance into Jehol reached Nanking, the Central Political Council, dominated by Wang Ching-wei, voted for a policy of "armed resistance without neglecting the methods of diplomacy," and telegraphed to the young marshal ordering him to send large reinforcements to Jehol. There was at this moment a wave of popular indignation against the young marshal on account of his passive policy, and Wang Ching-wei clearly felt that the moment had come for a trial of strength, not only with Chang Hsueh-liang, but with his nominal superior, Chiang Kai-shek, who even now was refusing to return to Nanking to discuss the situation with himself and his colleagues. On the 6th August, he called the local press correspondents together, brusquely announced his resignation of the post of President of the Executive Yuan, and then, without a word to his colleagues, left for Shanghai, whence, in a series of violently-worded telegrams addressed to the President of the Government, to General Chiang himself, and to others, he informed them that his resignation was due to his dissatisfaction with the policy of non-resistance

against Japan which had been adopted by the Chinese leaders, and charged Chiang Kai-shek not only with failing at every step to lift a hand against Japanese aggression, but also with making ever more and more outrageous demands on the Government Treasury. In resigning himself, he therefore called on the young marshal to resign likewise, "a step which would certainly be an inestimable blessing to China." The young marshal's reply to this onslaught was to telegraph to the Central Executive Committee to tender his resignation from his post of Peiping Pacification Commissioner. It was generally felt that if the young marshal were to be removed from Peiping at this moment, it would have a serious effect not only on the situation in the north, where the militarists grouped round Yen Hsi-shan and Feng Yu-hsiang would then form the dominating influence, but also at Nanking, since General Chiang Kai-shek's position would be seriously weakened by defection in the North. Strenuous efforts were accordingly made to get Wang Ching-wei to withdraw his resignation. As Wang would not give way, his "face" had to be saved, and accordingly an oriental solution was found. The post of Peiping Pacification Commissioner was abolished and superseded by a military committee, to be known as the Hopei Branch of the Nanking Military Council. General Chiang Kai-shek, as chairman of the Central Military Council, was to be ex-officio chairman of the new committee, too. After a suitable interval had elapsed, it was announced that, as General Chiang could not attend the meetings himself, Marshal Chang would act as his substitute. So, with a change of signboards, all continued as before. Wang, however, refused to be put off by this pretence, and maintained his refusal to return to the Government. The latter equally firmly refused to accept his resignation, and granted him three months' leave, on the understanding that the question of the appointment of a successor should await the convocation of the third plenary session of the Central Executive Committee. Wang, nevertheless, was really sick, and left for Europe in the latter half of October to seek medical treatment.

- 15. In the middle of September the two military commanders who have for some years been sharing the control and the revenues of Shantung came to blows. The protagonists were General Han Fu-ch'u, chairman of the Shantung Provincial Government and concurrently commander of the IIIrd Route Army, and General Liu Chen-nien, commander of the 21st Division and concurrently garrison commander of the Kiaotung Peninsula, including the port of Chefoo. General Han, who was the aggressor, alleged various reasons for his action, but there can be little doubt that the real motive was merely to eliminate an uncomfortable rival and make himself absolute master of the whole province and its revenues. The Central Government, whose sympathies were with General Liu (who had been regarded as a useful foil to the too powerful Governor of Shantung), and who could not but be exasperated by this very ill-timed exhibition of internal dissension, nevertheless steadfastly refused to be drawn into the quarrel, but exerted all its influence to prevent the outbreak of open hostilities. Han, however, while protesting his loyalty to the Central Government, steadily pursued his plans, isolated his weaker enemy in the mountainous heart of the peninsula, and, without encountering any serious resistance, occupied Chefoo. Then, having all the cards in his hands, he consented to listen to the peace talkers from the Central Government. The latter, faced with a fait accompli, had no option but to accept the situation, and, after a show of bargaining, Liu Chen-nien allowed himself and his forces to be transferred to Chekiang to participate in the anti-Communist campaign, and Han Fu-chu was left master of the whole of Shantung.
- 16. Almost at the same time, a similar situation arose in Szechuan. This province has not yet come within the orbit of the Central Government, and has remained one of the most backward politically of all the provinces of China, and a stronghold of feudal militarism. It was controlled, until the events which are now being discussed, by the two Lius—Liu Wen-hui (nominally chairman of the Provincial Government, with headquarters at Chengtu), and his nephew, Liu Hsiang (nominally Rehabilitation Commissioner for Szechuan, with headquarters at Chungking)—with a horde of subsidiary militarists of doubtful allegiance, Tien Sung-yao, Teng Hsi-hou, Yang Sen, and others. Liu Hsiang has for some considerable time watched his uncle with a very jealous eye, and, by means of his stranglehold on the river transport at Chungking, has successfully

prevented him from bringing in arms and munitions in any quantity. Fighting broke out between Liu Wen-hui and one of Liu Hsiang's henchmen on the 1st October. The remaining militarists, apparently without exception, rallied round Liu Hsiang, and a combined assault was made on Liu Wen-hui. The latter put up a vigorous resistance, but was outnumbered and outgunned. According to the latest reports received, he has been driven out of his stronghold at Chengtu, but fighting still continues. The situation is still obscure, and the details of these feudal conflicts are in any case immaterial, but Chinese public opinion holds Liu Hsiang the aggressor, and calls on the Central Government to punish him. The Central Government, however, here, as in Shantung and earlier in Kwangtung, being powerless to intervene effectively, has adhered to its policy of consolidating its power in the home provinces and refusing to dissipate its energies in costly military expeditions in remote regions.

- 17. The seat of Government was moved back from Loyang to Nanking on the 1st December, Loyang and Sian being, however, retained as "provisional" and "auxiliary" capitals respectively.
- From the 10th to the 14th December, the Second National Civil Affairs Conference was held in Nanking. It consisted of representatives of the various provincial and special municipal Governments, and considered schemes for the introduction of district autonomy and the reform of local administration. This was followed on the 15th December by the third plenary session of the Central Executive Committee. General Chiang Kai-shek returned to Nanking for the occasion, thereby signifying that the back of the anti-Communist campaign was broken, while the attendance of Sun Fo and others of the Cantonese politicians maintained the semblance of national unity to which so much importance is attached. The proceedings were on the whole uneventful, though two proposals were passed, which may have far-reaching importance if they are carried into execution. The first is that a National People's Congress be convened in March 1935 to draw up a permanent Constitution for the country in order to prepare the ground for the inauguration of constitutional government, and the other that before the end of 1933 a National People's Assembly be established in order to enable representatives of the people to participate in the government during the remainder of the period of political tutelage. The constitutional difficulty caused by the continuous absence from the capital of two, and sometimes all three, of the members of the Standing Committee of the Central Political Council was overcome by a resolution increasing the number of the members from three to five, and providing that, in the absence of members of this committee, members of the Standing Committee of the Central Executive Committee should act instead. This decision rendered it unnecessary to accept the resignation of Wang Ching-wei, who therefore continued to be "on leave."

(2) Manchuria and Dependencies.

(a) General.

- 19. The end of 1931 was marked by the virtual occupation of Manchuria by the Japanese military forces. The past year has seen the North-Eastern Provinces formed into a separate territorial entity under a virtual Japanese protectorate.
- 20. As mentioned in the report for 1931, the Japanese troops entered Chinchow in the early days of January, after they had forced the withdrawal of the Liaoning Provisional Government which was established there. This had been the last foothold of Chang Hsueh-liang's Administration in Manchuria. The only remaining challenge to the titular authority of the new Provincial Governments set up under Japanese influence at Mukden, Kirin and Tsitsihar was at Pin Hsien, some 50 miles to the east of Harbin, where the remnants of the old Kirin Provincial Government had taken refuge. In February an expedition was launched against Pin Hsien by the new Government of Kirin. This led to an attack on Harbin by the "old Kirin" troops dislodged from Pin Hsien, which in turn gave a pretext for the occupation of Harbin on the 5th February by the Japanese, who had hitherto not challenged the Russian interests in the Chinese Eastern Railway centred there. The Japanese then proceeded to engineer the establishment of an autonomous Government for the whole of Manchuria.

- 21. A conference was held at Mukden of officials nominally representing the provinces of Fengtien, Kirin, Heilungchiang and Jehol as well as two Mongol princes, which on the 18th February declared the independence of Manchuria from the Republic of China. (The declaration included Jehol, but this province has actually in no sense been brought within the new State, the local Tuchun, Tang Yu-lin, remaining in practice independent and outwardly maintaining his allegiance to China.)
- 22. On the 24th February the Constitution of the new State of Manchukuo was promulgated, and on the 9th March a Government was inaugurated at Changchun with the ex-Emperor of China, Pu Yi, as Regent.
- 23. On the 12th March the new Government addressed communications to the Powers requesting recognition, to which, as far as is known, no reply was returned except by the Japanese Government. The question of the recognition of the new State by Japan is dealt with under the heading of "Sino-Japanese Relations." At first only *de facto* relations were maintained; full recognition was finally accorded on the 15th September.
- The new Constitution provides for a system of yuans or councils— Legislative, Executive and Judicial and Supervisory—on the model of the Nanking Government. The Executive Yuan, however, comprises besides the various Ministries a Bureau of General Affairs, which controls the work of the ministerial departments. The personnel of this bureau is drawn from among the Japanese advisers, of whom a number are employed by the new Government. latter have issued a number of laws and ordinances during the year dealing mainly with administrative organisation. The control exercised by the Government over the country outside the main centres has, however, been severely limited by continuous internal disorders. These have been particularly serious in North Manchuria, where, after the capture of Harbin, the "old Kirin" troops and the Chinese Eastern Railway guards under Li Tu and Ting Chao started guerilla warfare down the eastern section of the Chinese Eastern Railway. In April General Ma Chan-shan, the ex-Governor of Tsitsihar, who, after his defeat in November 1931, had come to terms with the Japanese and had been made Minister of War in the new Government, revolted and threatened Harbin from the northwest. The "Manchukuo" army, composed of troops of the old Chinese armies who had transferred their allegiance to the new Government, proved generally unreliable when employed to deal with these attacks. The Japanese were compelled, therefore, to send troops against the insurgents and succeeded in the course of the summer in breaking up the main hostile forces, but were unable to wipe them out or to prevent repeated attacks on towns and railways, and by the end of the summer were practically confining themselves to the holding of important strategic centres, with the result that traffic on the eastern section of the Chinese Eastern Railway suffered almost continuous interruption, and by September travel on the south and west sections became so unsafe that British subjects were advised not to use the Siberian route to Europe. During August a series of attacks were also carried out on the South Manchuria Railway, which were, however, beaten off fairly easily, and there has been frequent skirmishing down the Peking-Mukden Railway, accompanied by rumours of intentions on the part of the Japanese to advance past Shanhaikuan or to invade Jehol. Neither threat had materialised at the end of the year, partly, no doubt, owing to the fact that the Japanese had been fully occupied coping with a sudden revolt which at the end of September broke out along the western section of the Chinese Eastern Railway. At Manchuli, Hailar and Chalandun the railway protection troops under their commander, General Su P'ing-wen, threw off their allegiance to Manchukuo, and for some two months almost the whole of Manchuria to the north-west of Harbin, with the exception of a small area round Tsitsihar, was in the hands of the insurgents. The problem of dealing with the revolt was complicated by Japanese reluctance to undertake military operations near the Russian frontier at the risk of giving offence to the Soviet Government, and by their fear that the Japanese residents of Manchuli and Hailar might, in the event of an attack, be massacred by the rebels. After some weeks of negotiation, however, the Japanese apparently obtained assurances that an advance up the Chinese Eastern Railway would neither give offence to the Soviet nor would endanger the safety of the Japanese prisoners held by General Su; and during the last weeks

of November a vigorous attack was launched on the insurgents. After an unavailing resistance, General Su was forced back to the Russian border, over which he escaped at the beginning of December with a few of his adherents. Such troops as were not killed or captured escaped into the wild country to the east of the railway, where they have presumably joined the hordes of "volunteers" who are operating against the Japanese. The Japanese Government applied for the extradition of General Su as a common criminal; this was refused by the Soviet Government, and at the end of the year he was stated to be returning to China via Europe.

- 25. Information is lacking regarding the financial circumstances of the new Government, whose possible sources of revenue must have been curtailed by disturbed conditions.
- 26. Soon after the establishment of the Government it was announced that the Mitsui-Mitsubishi group had granted them a short-term loan of 20 million yen, and steps were taken to obtain control of the salt and customs revenues administered by the Central Government services. On the 28th March the offices of the District Salt Inspectorate were forcibly taken over, and the Salt Gabelle in Manchuria was placed in charge of a Japanese adviser.
- The question of the customs was complicated by the foreign interests directly involved, which for some time deterred the Manchukuo Government from interfering with the administration. While laying claim to the bulk of the revenue, they indicated their willingness to allow the remittance to Shanghai of a fair proportion for the service of the foreign loans and indemnities, and privately put forward proposals to the Inspector-General for an arrangement whereby the customs should continue to function in Manchuria on this basis. The Chinese Government, however, refused absolutely to allow the Inspector-General to enter into any kind of understanding with the Manchukuo authorities. At the end of March the latter instructed the customs-collecting banks to pay over all revenue to banks designated by them. The banks demurred, but were eventually compelled to suspend remittances to Shanghai, and the revenue was held for the time being in suspense. The Manchukuo Government was, however, unable to interfere with the important Dairen revenues without the consent of the Chinese Government or the open assistance of the Japanese authorities. The question came to a head in June, when the Commissioner of Customs at Dairen, a Japanese, refused to remit revenue to Shanghai and was dismissed by the Inspector-General. The ex-commissioner thereupon commenced (with the connivance of the local authorities) to collect revenues at Dairen on behalf of the Manchukuo Government, and simultaneously the customs-houses at the Manchurian ports were forcibly taken over.
- 28. A certain proportion of the Manchurian customs revenue collected prior to the seizure of the customs-houses was, under orders from the Manchukuo Government, remitted to Shanghai in August, and in September the Manchukuo Minister for Foreign Affairs announced that the Manchukuo desired to pay her quota toward the service of indemnities and foreign loans secured upon the customs. Up to the end of the year, however, the Chinese Government had not taken advantage of this offer and had succeeded in meeting all these obligations themselves; it seems probable that, in doing so, they were actuated by a desire to avoid the possibility of the Powers being tempted to accept any offer from the Changchun Government which might hasten recognition of the new State.
- 29. In spite of threats of retaliation by the Chinese, no attempt was, however, made by either side to subject trade between China and Manchuria to customs duty until September, when the Manchukuo Government announced that China would be treated as a foreign country in this as in other matters and that duty would be levied on exports and imports to and from China accordingly as from the 25th September.
- 30. When considering retaliatory measures, the Chinese Government were at first in favour of treating Manchuria, for customs purposes, as a foreign country, and of imposing full duties upon Manchurian products. They finally decided, however, that to do so would weaken their political claim that Manchuria was still an integral part of China, and they therefore contented themselves with treating Manchukuo, from the fiscal point of view, as a Chinese province in

rebellion. Accordingly, by a Customs Notification dated the 24th September, the existing Chinese customs procedure was only modified to allow as far as possible for the collection in China of those duties on imports into Manchuria which would in normal circumstances have been collected at Manchurian ports; while Manchurian products imported into China continued to be taxed at the special low rates provided for native goods. In view of the fact, however, that in the Chinese view the Japanese had, by conniving at the seizure of the Dairer customs, invalidated the Sino-Japanese Customs Agreement of 1907, Dairen was henceforward treated as foreign territory, and goods shipped from or to Manchuria via Dairen were compelled to pay full duties.

31. The Postal Administration was later taken over in somewhat similar circumstances, after attempts by the Commissioner at Mukden to arrange a compromise had failed. The Manchukuo authorities announced their intention of introducing a separate stamp issue for Manchuria on the 1st August, and the Chinese Government thereupon instituted a postal blockade of Manchuria, and withdrew the postal staffs. The attempts of the Manchukuo Government to establish a Postal Administration of their own have so far been only partially successful, and the postal services in Manchuria, including the mail service between Europe and the Far East via Siberia, have been seriously disorganised as a result.

(b) South Manchuria Railway.

- 32. The financial year 1931–32 was the leanest in the history of the South Manchuria Railway. The elimination of competition from Chinese "parallel" lines, and Japan's departure from the gold standard, were not sufficient to offset the combined effects of the economic depression and of the dislocation of Manchurian trade, caused by the disturbed state of the country; and for the first time in its career the railway showed a loss—one of $3\frac{1}{2}$ million yen, as compared with a profit of $21\frac{1}{2}$ million yen in the previous year.
- 33. In June 1932 Count Uchida resigned from the presidency of the railway to become Japanese Minister for Foreign Affairs, and his place was taken by Count H. Hayashi, a member of the Japanese House of Peers, and a former Professor of Literature in the Tokyo Imperial University. Count Hayashi, who assumed office in August, is credited with strong views on the necessity for a policy of retrenchment, and the abandonment by the company of all unprofitable subsidiary enterprises.
- 34. It is understood that the double-tracking of the South Manchuria Railway line between Mukden and Changchun has been almost completed.

(c) Other Lines.

- 35. Little information is available regarding the conditions which prevailed on the purely Chinese lines in Manchuria during 1932; it can, however, be safely presumed that they were severely affected by the disturbed political situation, and that most of them degenerated from competitors, to mere subsidiaries, of the South Manchuria Railway. In several cases, indeed, of railways built with Japanese capital, loan defaults provided the Japanese authorities with convenient pretexts for foreclosing and assuming virtual control.
- 36. Work on Hulutao and the Taoan—Solun line has been suspended in order to push forward the construction of the extension of the Kirin—Tunhua line to Kainei on the Korean border; the line has already reached Chientao, and when it is completed communication will be established between North Manchuria and the ice-free port of Rashin. This line together with another—in process of construction—from La Fa on the Kirin—Tunhua system to Harbin should be completed by 1934, and will then not only facilitate the problem of concentrating Japanese troops, at short notice in North Manchuria, but will also draw away the trade of that region from the Chinese Eastern Railway.
- 37. Work on a line of purely commercial importance to link up the Tsitsihar-Koshan and Hulan-Hailun systems, and thus tap one of the richest areas in Heilungchiang, was begun early in the year, but was later suspended

owing to the floods and the necessity for concentrating every effort upon the rapid completion of the two strategic lines referred to in the last paragraph. The construction of this line will probably be resumed in the near future.

(d) Mongolia.

38. From the meagre information available, it would appear that no events fany considerable importance occurred in Outer Mongolia during 1932. There was a certain intensification, under Soviet guidance, of the anti-religious campaign, which provoked mutterings of revolt among the conservative elements of the population, but these are as yet too weak openly to challenge the authority of the "Young Mongol" Government at Urga. The hopes of these reactionaries, however, are pinned upon the Japanese, who have formed the large Mongol minority in Western Manchukuo, into the semi-autonomous Province of Hsingan with an organisation at once feudalistic and enlightened, and who, working westward from this base, appear to be spreading among the princes of Chahar, Suiyuan and Inner Mongolia proper the doctrine that escape from the twin evils of Russian or of Chinese domination can only be found in federation with Manchukuo.

(e) Sinkiang.

- 39. The effects of the economic depression, heightened as they were by heavy taxation and a disastrous fall in the local currency, caused widespread suffering and discontent throughout Sinkiang during 1932. Conditions, nevertheless, remained fairly peaceful, save in the north-east of the province round Hami, where a revolt of discontented Tungans, begun in the previous year, and assisted by lawless elements from the adjacent Province of Kansu, caused the Provincial Government serious concern, and at one time bid fair to constitute a threat to Urumchi itself. The Government, finding itself unable to suppress the revolt by force, is reported finally to have bought off the rebels with a large sum of money The country round Hami, however, remained disturbed for some time after the Tungans had officially proffered their submission, and direct communication with China was in consequence interrupted for the greater part of the year.
- 40. As a result of the commercial agreement concluded between the Union of Soviet Socialist Republics and the Provincial Government in the autumn of the previous year, a number of new Russian trading posts were established in the north of Sinkiang during 1932, while the Chinese authorities, well conscious of their military weakness, went to great lengths to conciliate the Soviet Government, and to deprive it of the slightest pretext for armed intervention in the province.
- 41. Relations between His Majesty's consulate-general at Kashgar and the local authorities continued to be excellent, and there was a notable tendency on the part of the latter to respect British extra-territorial rights more than they had done in previous years, and to refer to the consulate-general questions in which British Indian subjects were involved. His Majesty's vice-consul made an extended tour of the province during the summer, in the course of which he proceeded by invitation to Urumchi to interview the provincial chairman, Chin Shu-jen.

(f) Tibet.

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42. In the spring of 1932 the Sino-Tibetan hostilities along the Szechuan and Kokonor borders, which had originated two years before in a quarrel between the Tachi and Behru monasteries (see paragraph 51 of the 1931 annual report), assumed serious proportions. The truce concluded at Kanze in the previous autumn was disregarded by both sides, and after the Tibetans had scored certain minor successes, the Chinese, who had in the meanwhile been strongly reinforced from Chengtu, counter-attacked, and in the course of the summer drove the Tibetans back to the line of the Yangtze. At the same time Chinese Mahometan forces from Chinghai invaded the Kokonor. The Chinese advance caused extreme nervousness at Lhassa, and at the beginning of August the Dalai Lama appealed to His Majesty's Government in the United Kingdom to intervene. He urged that pressure should be brought to bear upon the Chinese Government to stay the

advance of their troops pending negotiation of all outstanding questions between China and Tibet, and suggested the formation of a close alliance between Tibet and India.

- 43. At His Holiness's invitation Colonel Weir, Political Officer in Sikkim, proceeded to Lhassa towards the end of August. On his arrival he was informed that the Tibetan Government placed themselves unreservedly in the hands of Hajesty's Government, and that they were anxious for the negotiation of a settlement with China on the basis of the unratified Simla Convention of 1914.
- 44. In view of the risk that the situation, if allowed to develop, might become a serious threat to the northern frontiers of India, His Majesty's Government agreed to intercede in the interests of peace; and it was accordingly suggested at Nanking that Sino-Tibetan hostilities should cease pending a satisfactory settlement of the principal issues outstanding between the two countries. The Chinese Government, however, in response to these representations, adopted the classic attitude that the dispute was a purely domestic one, in which His Majesty's Government had no right to interfere. Meanwhile, the Chinese had halted their advance at the Yangtze, and during September hostilities were practically at a standstill. At the beginning of October, however, the Chinese attack was resumed, and the Tibetans were again forced to retire. Consternation reigned at Lhassa, and the Tibetan Government, disappointed at what they regarded as His Majesty's Government's failure to assist them, talked of an appeal to the League of Nations. Colonel Weir's position at Lhassa became increasingly difficult and embarrassing; but the situation was to some extent relieved by the strong representations made by His Majesty's Chargé d'Affaires to the Chinese Government on his arrival in Nanking on the 6th October; emphasising the lively interest which His Majesty's Government took in any question which in any way threatened to affect the peace and stability of Tibet, he strongly urged that hostilities be suspended pending a settlement of the dispute, and informed the Chinese Government of His Majesty's Government's readiness to lend their good offices in the cause of peace. The Chinese Government, while refusing to admit His Majesty's Government's right to mediate in what they still persisted in regarding as a domestic quarrel, nevertheless informed Mr. Ingram a few days later that orders had been issued to the attacking troops to stay their advance. Hostilities along the Szechuan-Tibetan border were, in fact, suspended almost immediately, but this desirable result may well have been due not so much to the Government's orders as to the sudden outbreak of civil war in Szechuan Province.
- Meanwhile, the Dalai Lama had at last decided to take the advice given him by Colonel Weir in 1930 (see paragraph 56 of 1930 report), and remove one of the principal causes of all the trouble by lifting the ban upon the Tashi (Panshan) Lama's return to Tibet. In the early days of October many of the Tashi Lama's relations were released on bail from the prisons where they had languished since his flight from the country; while the Dalai Lama addressed to him through the intermediaries of the Indian Government and of His Majesty's Legation a conciliatory letter inviting him to return forthwith to The Tashi Lama happened by a fortunate chance to have arrived in Peking at the beginning of October (for the declared purpose of holding national prayer meetings for the salvation of China), and thus His Majesty's Chargé d'Affaires was, on his return from Nanking, able to deliver the Dalai Lama's letter to him in person. His Holiness expressed gratification and promised to reply to it as soon as the original text arrived, but, up to the time of his departure for Nanking in the middle of December to attend the forthcoming plenary session of the Central Executive Committee of the Kuomintang, the original letter had not reached Peking, nor, as far as His Majesty's Legation were aware, had any answer been sent to Lhassa. Meanwhile the Dalai Lama, who continued to display the greatest nervousness regarding the good faith and future intentions of the Chinese, renewed his appeal to the Government of India to intervene with a view to settling the dispute; but, in view of the Chinese refusal to entertain our offer of mediation, it was decided that nothing more could be done at the moment, but that we must first wait and see whether the Chinese genuinely intended to keep the peace. In consequence of this decision, Colonel Weir left Lhassa on the 1st December to return to Sikkim.

46. The southern portion of the Sino-Tibetan border remained fairly quiet throughout the year save for the area round Batang, which, as a result of a coup d'État, executed with Tibetan help, was seized at the end of February by the Kuomintang delegate deputed by the Central Government to assume control of the newly-constituted Province of Hsikang (see paragraph 52 of 1931 report). This individual—Wang T'ien-chieh or K'o-sang-tze-jen by name—did not long enjoy undisputed control of his new dominion, for, quickly falling out with his libetan allies, he was besieged by them in Batang for some two months, and when in August the siege was raised by the arrival of Szechuanese troops, he quietly disappeared.

(3) Communism.

- 47. With the outbreak of hostilities in Shanghai, the Chinese Government were forced to abandon the offensive against the Communist armies south of the Yangtze, which had been inaugurated with so much publicity in the previous summer; and the Communists quickly recovered the territory which had been wrested from them by the Government troops. In the south, however, Marshal Ch'en Chi-tang, who had been appointed by Nanking Bandit Suppression Commissioner for the South-West, undertook early in the year an offensive against the Communist hordes in South Fukien, and was meeting with some success, until he became involved in a civil war with Admiral Ch'an Chak, which necessitated the withdrawal of his troops from Fukien. At the end of May, however, there was some improvement in the situation. On the termination of the hostilities at Shanghai, the XIXth Route Army were sent to Fukien, where they set about clearing up the province in a systematic and businesslike manner. About the same time, Chiang Kai-shek, who had been appointed Commander-inchief of the bandit suppression forces for Honan, Anhui, and Hupei, proceeded to Hankow to reorganise the Government troops and to raise funds for a new anti-Communist drive; while Ch'en Chi-tang, having composed his differences with the Cantonese navy, was free to stem the southward advance of the Communists and to drive them back over the Kwangtung border into Kiangsi.
- 48. During the course of the summer, a series of conferences to consider the question of the Communist menace were held at Kuling under the presidency of Chiang Kai-shek, as a result of which it was reported in the autumn that an offensive on a large scale was to be undertaken against the Communists in Kiangsi; nevertheless, at the end of the year, most of the province, together with large areas in six other provinces of Central or South China, was under a form of Soviet administration, and the Communist menace was no less serious than it had been at the end of 1931.
- 49. The trial of the Noulens couple who were arrested for communistic activities in the International Settlement at Shanghai on the 5th July, 1931 (see paragraph 56 of 1931 report), was, owing to the hostilities in Shanghai and other causes, seriously delayed, and it was not until the 5th July, 1932, that the accused were brought before the Kiangsu Higher Court, sitting at Nanking. Prior to the trial the defendants went on hunger strike as a protest against the refusal of the Chinese Government to allow them the services of a foreign lawyer or the transference of the case to the Shanghai Higher Court; and considerable pressure was brought to bear by radical sympathisers upon the Ministry of Justice to stay the proceedings. As a consequence of the criticisms levelled against the Government's handling of the case, the Minister of Justice, and concurrently Minister for Foreign Affairs, Dr. Lo Wen-kan, tendered his resignation. This was not accepted, and the law was allowed to take its course. Finally, after a trial, which has been criticised as a travesty of justice, the prisoners were, on the 19th August, found guilty of endangering the safety of the State, and a sentence of death, later commuted to one of imprisonment for life, was passed upon them.

(4) Floods.

50. The Yangtze Valley remained comparatively free from floods during 1932. In Kwangtung and Shantung, however, minor inundations took place, while the most serious floods of the year occurred in the Sungari Valley in Manchuria. Traffic along the western section of the Chinese Eastern Railway

was for some time interrupted, while in Harbin and the surrounding districts many million dollars' worth of damage was done, and intense misery caused among the already poverty-stricken peasantry.

51. In Central China the National Flood Relief Commission was able on the 30th June to announce that its task had been almost completed. Old dykes broken in the previous year's floods had been repaired, thousands of miles of new dykes and roads had been constructed, and the Yangtze Valley was now in a better position than it had been for some time past to meet the menace of future floods.

(5) Banditry.

- In China proper only two cases of banditry involving British subjects occurred during the year. On the 27th February Communists raided the Breaker Point Lighthouse and abducted the British lighthousekeeper, Edwards, his Russian assistant, Andreyanov, and their respective wives and children. women and children were released a few days later, while the two men, for whom a large ransom was demanded, were carried off into the hills. Energetic representations were made at Nanking, Canton and Swatow, but without any tangible result, and in May Marshal Ch'en Chi-t'ang informed His Majesty's consul-general at Canton that his troops had captured a copy of a Communist proclamation announcing the execution of the two prisoners. At Swatow, however, the belief -shared by His Majesty's consul-persisted that the prisoners were still alive, and in July a Chinese emissary sent into the bandit country by His Majesty's consul reported on his return that the prisoners were well and that he had established contact with their captors. Unfortunately, however, at this stage, the emissary dropped out of the case and for some months no other means were available of communicating with the bandits. Another emissary was, nevertheless, despatched into the hills at the end of October. Meanwhile, the Kwangtung provincial authorities have persisted in their belief that the captives were executed not long after their capture. At the end of November His Majesty's consul, Swatow, reported that as a result of investigations it was believed that Edwards had died of injuries and his Russian assistant of illness during the autumn.
- 53. On the 12th May the Rev. H. S. Ferguson, a Canadian missionary engaged in flood relief work, was captured by Communist troops at Chengyangkuan in Anhui. Mr. Vice-Consul Graham, who was sent up into the district from Nanking in the hope of securing his release, was unfortunately wounded by Government troops who fired upon him in mistake and was compelled to return to Nanking. The Waichiaopu apologised for the incident, and assured His Majesty's Legation that there was every hope of securing Mr. Ferguson's release in the near future. Nevertheless, at the end of the year, despite frequent representations by His Majesty's Legation, Mr. Ferguson had not yet been set at liberty, and there was reason to believe that he had died in captivity some months before. The person responsible for wounding Mr. Vice-Consul Graham was sentenced to two years' imprisonment and two years' deprivation of civil rights.
- 54. On the 8th May Mr. G. Findlay Andrew, of the Flood Relief Commission, succeeded in obtaining the release of Father Sands, who had been captured by Communists in Hupeh in the previous August (see paragraph 131 of 1931 report).
- 55. The disturbed conditions which ruled in Manchuria—particularly in the latter part of the year—were reflected in the number of attacks which were made by bandits upon British subjects. On the 7th September Messrs. Mackintosh and Corkran and Mrs. Pawley were captured by bandits on Newchwang racecourse. Mr. Mackintosh subsequently made good his escape, but Mr. Corkran and Mrs. Pawley were held by the bandits for some six weeks and were only released on 20th October by the intervention of the Manchukuo and Japanese authorities after the payment of a ransom of about 135,000 dollars, 100,000 dollars of which was provided by the Manchukuo Government. On the 10th September Messrs. Hansell and Melhuish, respectively manager and sub-manager of the Harbin branch of the Hong Kong and Shanghai Bank, were attacked on the Harbin golf-course by bandits, who were only beaten off after a severe struggle in the course of which

Mr. Hansell was badly wounded in the arm; while on the 12th October another British resident of Harbin, Mrs. Woodruff, was murdered by bandits in an attempt to kidnap her children whom she was escorting to school. The comparative ease with which the bandits were able to perpetrate the crime in broad daylight and in a populous quarter of the town was in no small measure due to the cowardice and inefficiency of the Harbin police; and as a result of strong reprentations made by the consular body locally and by His Majesty's Embassy in Tokyo to the Japanese Government, it was subsequently announced that the Harbin police force was to be thoroughly reorganised. The conditions at Harbin became so appalling owing to the complete inadequacy of the local police and the constant danger of acts of armed violence to which the British community was exposed that the latter passed a resolution calling for a small international police or military force to guarantee security for foreigners residing in the town.

(6) Military Operations.

(a) Introductory.

- 56. The most remarkable feature of the year was the resistance offered by the Cantonese XIXth Route Army to the Japanese invasion at Shanghai. The disgraceful evacuation of Manchuria, whose troops were the best equipped in China, before a handful of Japanese regulars caused no surprise, but the fact that the ill-supported Cantonese could withstand for six weeks the assaults of the paramount army in the Far East has sent a wave of enthusiasm throughout the country. Money has poured in from all quarters to aid the volunteer movement in Manchuria, and the XIXth Route Army have been exalted into national heroes. It must be admitted that the type of country favoured the defence. Nevertheless, the fact that the Chinese stood at all was a revelation to their countrymen and has awakened in their breasts a hope that Manchuria may be recovered by force of arms. This is probably an absurd contention, but there is no doubt that the newlyfound spirit of resistance may cost the Japanese dear.
- 57. In Manchuria banditry has always been endemic. With the breakdown of the old Administration, interruption of communications and consequent difficulties in marketing produce, banditry in Manchuria has grown out of all proportions. On the ejection of Chang Hsueh-liang a large proportion of his troops were left leaderless. Some took service under the new Administration, but their loyalty has proved a very doubtful quality. Furnished with money from China they were ready at any moment to return to their old allegiance. To them must be added the so-called volunteers, drawn from units all over the country and despatched through Jehol to co-operate with the remaining elements of the old army. Other forms of bandits are the religious societies like the "Big Swords," "Red Spears," "Great Souls." Based in the mountains, they harry the country-side and retire to their fastnesses when pursued. The Japanese have adopted the policy of stationing troops at vital centres of communication and of attempting to deal with the guerillas by bombing planes. It is difficult to say what amount of cohesion and mutual support exists between the various bands, but all are imbued with a hatred of the invader, and all seem determined to create a state of chaos in the country. Even given good leaders, the task confronting the Japanese will be one of extraordinary difficulty, and it will be some time before Manchuria brings in any return for the money expended.
- 58. It must not be imagined that Manchuria holds any monopoly of banditry. China herself has a similar problem. Whereas the Japanese stigmatise all anti-Manchukuo troops as bandits, the Chinese call all their bandits, Communists or Reds. The subjugation of these anti-Government forces has been for years a problem which has defied solution. Many attempts have been made to suppress them, but until recently no success has attended the efforts. In fact, the Reds have usually succeeded in either defeating or suborning the troops sent against them. Their supply of arms came almost entirely from this source, and to leave them in contact with a punitive expedition was a certain means of replenishing their magazines.
- 59. In the month of August, however, Chiang Kai-shek concentrated the larger part of his troops around Hankow, and by a series of determined drives [8425]

cleared a large part of Hupeh and the Anhui borders. In this connexion it is interesting to note that a Government ordinance has been promulgated for reallotting land to serving soldiers, and placing districts under the control of brigade and division commanders. Land which has been uncultivated owing to the flight of the original owners, or whose title deeds have been destroyed and boundary-marks removed by the Reds, is being reallotted by a commission. Soldiers and their families are encouraged to settle, and men are only permitted to marry local girls, or select wives from their own villages. Previous efforts and dislodge the bandits only succeeded in driving them into their mountain bases, and on the withdrawal of the troops they descended once more and harried the plains. The new settlement scheme is designed to prevent a return of the scattered hordes, and presumably finally to arrange for the disbandment of time-expired men.

- 60. The bandit situation in Kiangsi has not been so satisfactorily handled, and there is a suspicion that the Cantonese are reserving themselves for a struggle with Chiang Kai-shek. Early in March a concerted drive against the Reds in Southern Kiangsi and Western Fukien was arranged, and as far as the Kwangtung army was concerned, achieved some success. Chen Chi-t'ang's efforts to gain complete control of the forces in the province led, however, to a rupture with the navy and Admiral Chen Chak. This internal strife brought the Kwangtung drive against the bandits in South Kiangsi to a halt. In Fukien the 49th Division collapsed and the Reds arrived within striking distance of Amoy. Meanwhile Communist columns retaliated for the penetration of their strongholds by invading Kwangtung from the north and a serious situation arose in the Nankang, Sinfeng and Namyung districts, where they had considerable successes against the regular troops. In July a number of divisions had to be rushed to Kanchow to relieve the situation. A combined drive was arranged to take place with the assistance of the XIXth Route Army. The latter, when withdrawn from Shanghai, were sent to Foochow, and the Communists who had been threatening Amoy withdrew to their own areas in Southern Fukien. Although the Kwangtung troops were reported to have made progress, it appears that the XIXth Route Army has contented itself with settling down to occupy the Min Valley, leaving the Communists much to their own devices.
- 61. On the 17th September, two days after the Japanese recognition of Manchuria, when it might have been expected that Chinese of all classes would sink their common differences, Han Fu-chu, the chairman of Shantung, considered it opportune to start a private war with Liu Chien-nien (see Internal Political Situation, General).
- 62. During the year hostilities broke out on the Sino-Tibetan border (see paragraphs 42-48).

(b) Shanghai Incident.

- 63. The events leading up to and a brief account of the outbreak of hostilities at Shanghai are set out in paragraph 97.
- 64. At the end of three or four days' fighting the Japanese authorities discovered that the task of clearing the Chinese from the vicinity of Shanghai was beyond the power of the navy and appealed to Tokyo for military reinforcements. In the meantime the navy bombarded the forts at Woosung, which defend the entrance to the Whangpoo River. An expeditionary force, consisting of the 9th Division and a mixed brigade from the 12th Division, was mobilised in Japan. The latter was despatched to China in warships on the 6th February. On the following day a landing was effected at Woosungchen with a view to taking the forts in the rear, but determined opposition prevented an assault being made.
- 65. The 9th Division arrived off Shanghai on the 13th February. A portion of the troops were detached to assist the mixed brigade in their task of reducing the forts, whilst the remainder were landed at Shanghai itself, taking over from the marines, who were holding the main front. On the 20th February the 9th Division launched an offensive against Kiangwanchen, a village half-way between Woosung and Shanghai. The Japanese here discovered the immense power of a defence strengthened with machine guns and barbed wire. The country was unsuitable for tanks and artillery observation, and the attack made little progress in proportion to the casualties incurred. Reinforcements had to

be called for, and the 11th and 14th Divisions were mobilised in Japan. These reinforcements arrived on the 29th February, and the 11th Division landed at Liuhochen on the Yangtze River to take the Chinese positions in reverse. The 9th Division and the 24th Mixed Brigade continued their frontal attack westwards on the 1st March, whilst the 11th Division threatened the Chinese flank. A detachment occupied the Woosung forts, which were evacuated by the Phinese on their rear being threatened. The Chinese retired in an orderly manner to the line Taitsang–Kunshan, where they remained until withdrawn from the Shanghai area. Throughout the operations their military action was entirely defensive and no counter-attacks on a large scale were attempted. No use was made of their air arm, such as it is, with the result that the Japanese forces maintained a commanding superiority in the air throughout the period of hostilities.

(c) Manchuria.

- 66. The withdrawal of the regular Chinese forces of Chang Hsueh-liang within the Great Wall on the 5th January left the Japanese with the impression that the main obstacle to the consolidation of the new State had been removed. They were, however, speedily disillusioned, and as they themselves admit the Japanese army had to face an aftermath which proved anything but pleasant or easy to deal with. In one of their propaganda publications they state that it is customary for a Chinese army, when defeated, to leave behind it troops of inferior quality, so that they may combine with local bandits for the purpose of harassing the enemy's rear. The suppression of banditry in the evacuated region has proved rather a costly affair.
- 67. The first major operation was the outcome of an engagement between the Kirin troops of General Hsi Hsia and the anti-Manchukuo forces who still remained loyal to Chang Tso-hsiang, the late Governor. The latter set up a new Government at Pinhsien, north-east of Harbin. Attempts to win over the anti-Manchukuo elements failed, and an advance by General Hsi Hsia's troops resulted in a struggle for Harbin. It was soon evident that the newly-formed Chinese army was no match for the anti-Manchukuo forces, and the Japanese 2nd Division was despatched to their assistance. General Ma Chan-shan, who had originally been sent to Harbin to mediate between the Chinese forces, now went over definitely to the opposition, and has since remained the most powerful partisan leader of the irregulars.
- 68. Harbin was captured after three days' fighting by the Japanese, and the anti-Manchukuo forces retired on Pinhsien and Hulan.
- 69. In April a considerable number of the old Kirin troops concentrated east of Harbin. The Japanese decided to disperse them and clear the region between Wukimiho and Fangchen. Two columns from the 2nd Division were entrusted with this task, one proceeding along the Chinese Eastern Railway and the other direct to Fangchen. After several minor engagements the two columns united and took up a defensive position with the intention of inducing the enemy to attack. The latter ran out of gun ammunition and the Japanese advanced and dispersed them, and then withdrew to Harbin.
- 70. Ma Chan-shan, however, reassembled his scattered forces, and by continuing to harass the Japanese line of communications compelled the Japanese authorities to despatch reinforcements. At the beginning of July the 14th Division at war strength was shipped to Manchuria from Shanghai. Operations were opened against him in the Hailun-Hulan area, part of the division being stationed near Koshan and Tsitsihar. The 2nd Division formed the garrison of Kirin and undertook the protection of the work on the Tunhua Railway, leaving one brigade, the Amato, at Tsitsihar, until the campaign against Ma had been terminated. The 10th Division sent one brigade to the Lower Sungari and another to the eastern section of the Chinese Eastern Railway. By the end of July the drive against Ma was brought to a successful conclusion. His troops were defeated with heavy loss and he himself was reported killed.
- 71. The Japanese then concentrated on guarding vital points of communications along the railways, trusting to their intelligence service to discover any large concentration of irregulars and to their aeroplanes to disperse them.

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- 72. Efforts to destroy irregulars by the employment of flying columns produced extremely small results. The high crops in the plains formed excellent cover from air and ground observation, and the Japanese wore themselves out with no visible result. They accordingly confined themselves purely to the defensive, relying on the arrival of the Manchurian winter to facilitate their task.
- 73. At the end of July an incident occurred which nearly provoked further conflict with China proper. The Japanese have always regarded the Province of Jehol as part of Manchuria. Its Governor, Tang Yu-lin, found himself in the unenviable position of being bullied by both sides. As long as the province was under the influence of Chang Hsueh-liang a portion of its opium revenues found its way into his coffers. It also remained the only State through which men and supplies to feed the insurgent movement in Manchuria could pass. The Japanese had no intention of employing their regular troops in the mountainous country where their communications would be dangerously exposed. They had, on the other hand, every interest in attempting to win over the Governor, divert revenues to Manchuria and close the door against the volunteers, who by this time were becoming a serious menace. Negotiations were, therefore, opened with Tang Yu-lin to purchase his allegiance. During the course of these negotiations a party of volunteers, operating in the Peipiao district, captured a Japanese officer named Ishimoto, who is strongly suspected of being one of their agents. The branch line from Chinchow to the mines was damaged at the same time by a raiding party. The Japanese general commanding the 8th Division at Chinchow despatched two columns of about a regiment apiece and an armoured train to effect the release of Ishimoto. These troops were engaged with volunteers and a brigade of Tang Yu-lin's, and crossed the frontier at Chaoyangssu. Aeroplanes were sent to bomb Chaoyang. Ishimoto's release was not effected, but the advance of even two regiments to the frontier was sufficient to alarm the Chinese authorities in Peking. Fearful lest Tang Yu-lin should go over to the enemy and that the frontier of Manchukuo would be extended to within 40 miles of Peking, the young marshal ordered four brigades of infantry and two of cavalry up to the Great Wall between Kupeikou and Hisfengk'ou. This move had a sobering effect on Tang and certainly checkmated the Japanese scheme for absorbing the province by purchase. The Japanese then threatened to attack Peking, should any of the North-Eastern Army cross the frontier of Jehol, but there is very little doubt that they had no idea of involving themselves in a campaign in China proper with an unlimited objective. The young marshal was certainly in a most difficult position. Any attempt to force the hand of Tang Yu-lin by sending troops into Jehol was likely to bring him into immediate conflict with the Japanese, who were only too anxious to secure his elimination and the establishment of an Administration in North China favourable to Japan. On the other hand, a policy of inaction was certain to invite attack from his political adversaries. He therefore elected to encourage the volunteer movement without openly committing himself. This brought upon him the wrath of Wang Ching-wei, who impeached him in most violent terms. The outcome of the political upheaval which ensued was, however, to leave the control of the forces in the North much as it was before.
- 74. It is difficult to secure any exact details of the organisation of the volunteers. Money has been subscribed all over the country and from Chinese abroad, and an administrative office exists in Peking. Men from various parts of the country are concentrated at Hsifengkou (where the Luan River passes through the Great Wall), and are equipped for guerilla warfare. They are mostly armed with pistols, and a long knife slung over their backs. They then are passed through Jehol into the Tungliao district. Some co-ordination of their efforts has been effected, and there was an intensification of their activities in many parts of Manchuria about the date of the recognition of the new State by Japan. Much damage was done at the Fushun Colliery, and systematic train wrecking ensued.
- 75. West of the Great Khingan Range, which forms the strategic frontier of Manchuria, the Japanese have been content to leave the policing to reformed Chinese troops. Great efforts have been made to win over the Princes of Inner Mongolia, and a frontier State, running from Heilungkiang to Fengtien, has

been demarcated and given the name of Hsingan. The response from the Mongols being favourable, and the fact that the Barga Mongols were strongly opposed to the old régime, probably lulled the Japanese into a sense of false security. seem to have been quite unprepared for the sudden revolt of General Su Ping-wen, commanding the Railway Police Forces, who on the 27th September declared his allegiance to Chang Hsueh-liang and imprisoned all Japanese in his area. In action which occurred at Fuliardi, Su's troops made use of heavy artillery, which led to the supposition that the Soviets, if not actually assisting them with arms, were at any rate not averse to selling munitions. The Japanese were loath to adventure west of the mountains to chastise the rebels, and for some time contented themselves with attempting to obtain the release of their nationals by negotiation. Exactly two months after the defection of Su P'ing-wen they began an offensive westwards from Tsitsihar, with a brigade as main body and a strong advanced guard of motorised infantry sweeping to the north to outflank Su's rearguard under Chan Tien-chu. A column was sent to Solun to prevent the rebels breaking away to the south. On the 1st December the Japanese captured Chalantun with little resistance, and successively occupied Taian, Neiho, Anta and Paichuan, effectively clearing the plains of Heilungkiang. Su P'ing-wen made no real effort to hold the line of the Khingans, and on the 3rd December the Japanese seized Pukoto and occupied both ends of the tunnel, which was found practically undamaged. Su P'ing-wen and his staff fled by train across the frontier on the 5th December, and was disarmed by the Soviet Frontier Guards. on the same day the Japanese occupied Hailar, after considerable aerial bombing, and on the 6th entered Manchouli. The revolt thus ended in an inglorious retreat, the moment the rebels were confronted with regular Japanese troops.

76. East of Mukden a drive on a considerable scale took place in October to rid the Province of Kirin of the elements of the old army and remove the menace to the construction of the Tunhua line, which was being considerably interfered with. This object was successfully accomplished, and the line for 40 kilom, east of Tunhua was opened to traffic on the 1st December.

(d) Chiang Kai-shek's Anti-Communist Campaign.

- 77. When Chiang Kai-shek started his operations against the Communists north of the Yangtze, the situation had become extremely serious. The forces to which he was opposed consisted of the IInd Red Army Group under Ho Lung, based on the district city of Kienli, and the IVth Red Army, on the borders of Hupeh, Anhwei and Honan, at Loshan and Kwangchow. Hankow was practically surrounded, and the railway communications with the north were badly interrupted by raids on the line. For the last three years Government troops have been attempting to suppress the IVth Red Army, but any determined efforts to dislodge them simply resulted in their dispersing to their stronghold in the Ping Ling Mountains, whence they returned as soon as their adversaries were withdrawn. By propaganda, bribery and, in some cases, by fighting, they have succeeded in overthrowing most of the troops sent against them, and increasing in numbers and armament at almost every engagement.
- 78. On the arrival of Chiang Kai-shek in Hankow all bandit suppression activities were placed under his command. The Government troops were divided into three columns. By a concerted drive from Hankow westwards and across the river northwards, the Hung Hu district was cleared of Ho Lung's troops. A party of these broke away to the south and threatened Shasi, where the Szechuan troops, who were supposed to be co-operating, gave a very poor account of themselves. They were finally driven off by some of Chiang's own divisions. The main body retired to the north-west after a severe defeat. On the 12th July the 4th Division, attached to the right column, recaptured the Hochiu district, and previous to this operation Cheng Yang Kuan and Lu An in Anhwei were cleared and the Reds driven into the mountains in Eastern Hupeh. Most of the bases of the Reds in this district have been occupied by Government troops, and an attempt has been made to preserve them by creating a local militia system and granting land to serving soldiers under military control. Chiang has dealt with a heavy hand with cases of cowardice on the part of subordinate commanders, a number of whom have been executed.

(e) Szechuan War.

79. (See section on Internal Political Situation—General.)

II.—Foreign Relations.

(1) United Kingdom.

(a) General.

- 80. Sino-British relations continued on a satisfactory footing during the year save for the question of Tibet, which is dealt with in another section. No major question formed the subject of negotiation between His Majesty's Government in the United Kingdom and the Chinese Government.
- 81. Land questions continued to present certain difficulties, and while in the case of the Asiatic Petroleum Company's wharf frontage at Pootung a satisfactory settlement was after several years of fruitless negotiation at last reached in the autumn of 1932, at Amoy and Swatow the question of foreshore rights and reclamation, as affecting land belonging to British subjects, was still under negotiation.
- 82. In view of the inclusion of prominent Cantonese in the new Chinese Government formed in Nanking at the beginning of the year, British underwriters were released from their undertaking not to insure shipments of arms destined for China (see paragraph 136 of 1931 report).
- 83. An acute shortage of funds at the Chinese Admiralty prevented the British Naval Mission under Commodore Baillie-Grohman (see paragraph 139 of 1931 report) from achieving any satisfactory results during the year. Commodore Baillie-Grohman, on more than one occasion, experienced no little difficulty in obtaining payment of his salary, and when at the end of the year the question of his successor was raised with the Minister of Marine, the latter stated that, while he was anxious for the mission to be continued in its present form, it might be necessary to allow a period of a few months to elapse between the departure of Commodore Baillie-Grohman and the appointment of his successor, in order to give time for funds to accumulate for the payment of salaries, &c.
- 84. As in former years, the unauthorised occupation of British mission premises by Chinese authorities or troops necessitated representations on more than one occasion to the Central Government. In particular, the case of the Anglo-Chinese College at Swatow, which was first seized by the municipal authorities in 1926, and which was later, despite frequent protests, turned into a municipal school, formed the subject of repeated representations by His Majesty's Legation; at the end of the year, however, this case still remained unsettled. On the other hand, in Szechuan a satisfactory settlement of the long outstanding case of the occupation of some Church Missionary Society property at Mienchow was obtained by local negotiation.
- 85. In September the attention of His Majesty's Chargé d'Affaires was drawn to a tendency recently displayed by the Ministry of Finance to supersede British subjects employed in the Salt Inspectorate, and to replace them by American nominees of the American Associate Chief Inspector, Mr. Cleveland. In view of the large British interests in the loans secured on the salt revenues, His Majesty's Chargé d'Affaires, during his visit to Nanking in October, took up the matter both with the Minister for Foreign Affairs and with the Minister of Finance, pointing out that the suppression for no good reason of capable English officials of the Salt Administration would create a most unfavourable impression in England.
- 86. On the 22nd July a note, dated the 18th July, was received from the Waichiaopu in reply to His Majesty's Legation's note of the 8th December, 1931 (see paragraph 138 of 1931 report), reaffirming the Chinese Government's decision that limits within which the pursuit of smugglers could be effected should be 12 nautical miles. The matter was referred to the Foreign Office for a decision.
- 87. The passport regulations introduced by the Chinese Government in May 1931 (see paragraph 141 of 1931 report) have until now worked fairly smoothly as far as British subjects are concerned, and there has been a steady and

satisfactory tendency to adopt a definite and uniform system of passport control at Chinese ports of entry. As regards travel in the interior, there would appear to be a movement on foot to compel foreigners to carry passports when travelling between treaty ports in China. His Majesty's Legation are not in principle opposed to the introduction of this procedure.

- 88. The administration of Weihaiwei continues to be satisfactory, although the local Chinese authorities were severely hampered by the suspension of the monthly grant of 15,000 dollars, which had previously been made from the national exchequer. Despite drastic economies and reductions in official salaries the funds available from local sources are not sufficient to defray the cost of maintaining the administration of the territory at the high standard set during the first year after rendition. A certain deterioration has already begun, and it is the opinion of His Majesty's consul that, failing a resumption of the Central Government grant, only reorganisation can save the territory from eventual bankruptcy or a decline to the comparatively low level of administrative efficiency which prevails in the rest of Shantung.
- 89. On the 22nd January a note was sent in to the Waichiaopu by His Majesty's Legation, formally presenting, on behalf of John Thorburn's parents, a claim for £1,000 on account of the expenses to which they had been put in their endeavour to ascertain the truth as to their son's fate and of the mental suffering involved (see paragraph 144 in 1931 report). Further representations were made personally by His Majesty's Minister, both to the Minister for Foreign Affairs and the Minister of Finance, as a result of which the Chinese Government on the 23rd February made a compassionate grant of £1,000 to Mr. Thorburn. This sum was accepted by the latter in full settlement of his claim.

(b) Interference with British Shipping.

- 90. Few cases of actual firing on British shipping occurred during 1932, and the only incident of the kind which had any serious repercussions was the dropping of bombs by one of Marshal Chen Chi-tang's aeroplanes near H.M.S. Moorhen off Wangmun on the 26th June. It seems clear that the incident occurred owing to the aeroplane mistaking H.M.S. Moorhen for one of Admiral Ch'an Chak's rebel ships, and satisfactory apologies were received both from the Nanking Government and the provincial authorities.
- 91. The position as regards the unauthorised searching of British vessels for opium, arms, &c., by Chinese armed police and soldiery continued during 1932 to be far from satisfactory. In reply to the vigorous representations made by His Majesty's Legation in connexion with the boarding of British vessels at Kowan (see paragraph 148 of 1931 report), the Waichiaopu early in the year stated that measures had been taken to obviate the occurrence of such incidents in future, and that the Executive Yuan had issued strict instructions to the authorities concerned to observe the proper and recognised procedure when undertaking searches of foreign shipping. A genuine attempt to enforce these instructions would appear to have been made, and for some months no cases occurred of armed parties attempting to board British vessels in an unauthorised manner. Early in July, however, the s.s. Woosung while lying alongside the French concession at Shanghai and later when proceeding to Pootung was, without warning, boarded and searched for opium by armed river police of the local Public Safety Bureau. His Majesty's consul-general immediately lodged a protest with the Mayor of Greater Shanghai, reminding him of the assurances given to His Majesty's Legation earlier in the year; while similar representations were made at Nanking. His Majesty's Legation were assured that steps had been taken to prevent the recurrence of such incidents, but nevertheless on the 6th August river police at Shanghai, without warning, again boarded a British vessel—the s.s. Nganking—and attempted to carry out a search. Their unauthorised activities were, however, interrupted by the arrival of His Majesty's shipping vice-consul, and after some argument they were induced to leave. Despite fresh protests, both locally and at Nanking, several further attempts were made during September by the river police at Shanghai to board British vessels, while on the 6th October the s.s. Suiwo was searched for bandits at Kowan, and two Chinese were removed from the ship by the search party. His Majesty's Chargé d'Affaires, who was at Nanking at the time, addressed a strong protest to the

Waichiaopu, which elicited the usual valueless assurances. Meanwhile searches of British shipping continued at Shanghai, while at Kowan interference with British vessels had become so serious that it had been found necessary to station a gunboat there at intervals. At the end of the year there was still no marked improvement in the situation, nor did there seem much likelihood of any taking place so long as the local authorities continued so openly to ignore the injunctions of the Central Government.

(c) Kuomintang in Malaya.

92. As a result of the strong measures taken by the colonial authorities, the activities of the Kuomintang in Malaya would appear to have been considerably reduced during 1932. No specific cases of infringement of the agreement concluded in April 1931 (see paragraph 150 of 1931 report) between His Majesty's Minister and Dr. C. T. Wang were brought to the notice of His Majesty's Legation. The Colonial Government, however, had on more than one occasion reason to complain of attempts, inspired from Nanking, to institute an anti-Japanese boycott, and to collect funds for General Ma Chan-shan, under the guise of "Flood Relief."

(2) Canada.

- 93. At the beginning of 1932 Mr. Paul Sykes, formerly Canadian Trade Commissioner in Hong Kong, was appointed to the newly-created post of Trade Commissioner for Manchuria with headquarters at Dairen. Mr. Eugene Duclos was appointed to succeed him as Trade Commissioner for Hong Kong and South China.
- 94. Early in the history of the present anti-Japanese boycott there had already been interference by the boycott organisations with the import into and sale in China of Canadian dried fish (see paragraph 155 of 1931 report). The ground on which the boycott organisations attempted to justify this interference was that the Canadian dried fish industry was largely Japanese-owned. In response to urgent representations from His Majesty's Legation, the Waichiaopu gave assurances that no further consignments would be interfered with, but the fish continued nevertheless to suffer boycott in many parts of China. Renewed representations met with no better success, the local authorities proving unable to restrain the boycott associations, and the latter refusing to accept assurances of the most categorical kind that the fish was caught, dried and packed by British labour employed by British capital. It is hoped, however, that as a result of further vigorous representations made at Nanking in October some improvement in the situation may be expected during the 1932–33 winter season—the period of the year when in normal circumstances the largest sales in China of Canadian dried fish are made.

(3) Japan

- 95. The tension in Sino-Japanese relations resulting from the seizure of Manchuria by the Japanese in the autumn of 1931 has eclipsed all other events in China during the year. The situation has, in fact, been one which in the normal relations between two Powers must logically have led to war. That neither side has actually taken the step of breaking off relations is because China is too hopelessly weak to take up the challenge and has had perforce to rely on the influence of the League of Nations and of world opinion in general to restrain Japan. Japan, on the other hand, who has not hesitated to prosecute her objects by warlike methods when necessary, has nothing to gain by a declaration of war, which would be likely to intensify the generally unfavourable repercussions which her high-handed actions have evoked in the opinion of the world.
- 96. At the end of 1931 the Japanese military forces, who had advanced step by step since the clash of the 18th September on the pretexts of protection of Japanese interests and military necessity, were in possession of all the principal strategic points in Manchuria except Harbin. Early in 1932 they availed themselves of a similar pretext to round off their position by the occupation of the latter town, which they entered on the 5th February. They then proceeded

with the design, which it had been for some time evident that they entertained, of setting up an independent Government of Manchuria which should be an instrument for the administration of the country under Japanese influence, and should at the same time regularise the position of the Japanese troops in Manchuria by acquiescing in their presence. The new State of Manchuria, or "Manchukuo," was established on the 18th February and the "Young Emperor," 'You Yi, installed as Regent on the 9th March. (A fuller account of these events is given in the section on Manchuria.) The Chinese Government protested to the Japanese Government in a note dated the 24th February holding Japan responsible for "illegal organisations" set up in territory unlawfully occupied by the Japanese. The Japanese Government, however, persisted in disclaiming all responsibility for the independence movement in Manchuria.

- In the meantime a crisis had arisen at Shanghai. The anti-Japanese boycott, which was China's retaliation to the Japanese action in Manchuria, was felt as a serious blow by Japan and was particularly active in Shanghai. A local anti-Japanese society was formed which intimidated merchants, confiscated Japanese goods, and in general indulged in anti-Japanese activities, for which, though they transgressed the law, no redress could be obtained in the Chinese courts, which did not dare to sentence so-called patriots. On the 18th January five Japanese, including two priests, were assaulted by a Chinese crowd and two of them seriously injured. The Japanese consul-general protested to the Mayor of Shanghai and demanded: (1) An official apology for the attack on the priests; (2) the punishment of the assailants; (3) compensation; (4) the suppression of all anti-Japanese organisations; and in the meanwhile Japanese naval reinforcements were rushed to Shanghai. At first it seemed that the matter would be settled, for the Chinese seemed prepared to make amends and the attitude of the Japanese consul-general was conciliatory, but the Japanese naval authorities were evidently determined to strike a blow which would crush the boycott. On the 27th January the Japanese consul-general's demands were renewed in the form of an ultimatum, and the Japanese Commander-in-chief made it known that failing compliance he would "take drastic action." The authorities of the International Settlement accordingly declared a state of emergency. On the afternoon of the 28th January the mayor accepted the demands. Nevertheless at midnight a Japanese landing party advanced to the perimeter assigned to them in the Hongkew district under the joint defence scheme of the international forces, and, coming into contact with Chinese troops outside the borders of the settlement, attempted to dislodge them and became engaged in hostilities which turned Shanghai into a battlefield for five weeks. The Japanese afterwards maintained that they had merely acted in accordance with the International Defence Scheme in advancing to the positions assigned to them; but the circumstances in which their night attack was carried out after the Chinese acceptance of their ultimatum made it clear that they were out to provoke a clash.
- 98. Details of the ensuing military operations are given in paragraphs 64 and 65. The resistance put up by the Chinese troops of the XIXth Route Army, who were opposed to them, came as a surprise to the Japanese, whose forces proved at first quite insufficient for the task they had undertaken, and for a time there was a danger that the Chinese would drive them back into the settlement. In the meantime attempts were being made by neutral parties (in which the British authorities generally took the lead) to bring about a cessation of hostilities. On the 29th January a truce was arranged on the initiative of the British and United States consuls-general, which was observed with intermittent violations for some days. Mr. (now Sir John) Brenan then put forward a proposal for the establishment of a neutral zone between the combatants, and His Majesty's Government supported the proposal and agreed to allow British troops to share in the policing of such a zone. The Chinese Government agreed under pressure from the British and United States representatives in Nanking to accept the proposal in principle, but on the 2nd February the Japanese in Shanghai announced that their Government had rejected it, and recommenced shelling the Chinese positions in Chapei, while their warships bombarded the Chinese forts at Woosung.
- 99. On the 31st January the Japanese had increased their naval force at Nanking, presumably as a demonstration against the Chinese Government, and [8425]

on the same day the latter, in order to remove themselves as a body from the reach of this kind of pressure, announced the transfer of the capital to Loyang, although individual members of the Cabinet remained in Nanking. On the night of the 1st February the Japanese warships fired several shells into the city (probably as the result of an alarm), but the ensuing tension did not lead to any

further developments.

- the Chinese and Japanese Governments by the British, United States and French representatives at Nanking and Tokyo, on the basis of the cessation of acts of violence and hostile preparations, the withdrawal of the combatants from points of contact and the establishment of neutral zones, these steps to be followed immediately by negotiations to settle all outstanding difficulties in the spirit of the Kellogg Pact and the resolutions of the League Council, without prior reservations and with the aid of neutral observers or participants. These proposals were accepted by the Chinese Government; but the Japanese Government, while not giving an unqualified acceptance to the other points, flatly rejected the last point, on the ground that the Manchurian question was entirely separate from the Shanghai affair, and that they could not admit the participation of third parties in the discussion of the former.
- 101. Local attempts to bring about a cessation of hostilities continued at Shanghai, but broke down after the landing of reinforcements by the Japanese.
- 102. About this time an inspired statement was issued in Tokyo to the effect that the Japanese Government were considering proposals for the solution of the Shanghai question and the general problem of security in China, by the establishment of demilitarised zones 20 miles wide round Shanghai, Tientsin, Hankow, Tsingtao and Canton. This suggestion, which was apparently put out as a ballon d'essai by the Press Department of the Gaimusho, provoked great hostility in China and received no support from the other Powers, and it was afterwards disavowed; but it became evident later that the creation of a demilitarised zone at Shanghai was what the Japanese had in mind as the final solution of the situation which their action had brought about.
- On the 5th February His Majesty's Minister arrived in Shanghai, and began a further attempt to bring the Chinese and Japanese together, with a view to the cessation of hostilities, in which the United States Minister, and to a lesser extent the French and Italian representatives, were induced to co-operate. The Chinese Government had already under pressure defined their attitude to be that they would withdraw their forces if the Japanese troops were withdrawn to the The Japanese Minister, approached by Sir Miles Lampson, now agreed in guarded terms to the suggestion that the Japanese troops might be withdrawn from all territory occupied since the 31st December if the Chinese retired to a given distance, and an effort was made to persuade the Chinese to consider the evacuation of the Shanghai municipal area north of the Soochow Creek and west of the Whangpoo. These negotiations were once more ruptured on the 18th February by an ultimatum from the Japanese, who had meantime landed a division in and near Shanghai, demanding the withdrawal of the Chinese to a given line (which was more or less equivalent to that suggested by Sir Miles Lampson) within forty-eight hours. This was rejected, and the Japanese launched an offensive to the north of the settlement round Kiangwan. Their advance was again held up by the Chinese troops, who resisted with unexpected stubbornness; and it was not till the 3rd March, after a further two divisions had been despatched from Japan, that the Japanese succeeded in forcing their retirement to a line roughly corresponding with that laid down in their ultimatum of the 18th February.
- 104. In the meantime the president of the League Council had put forward at Geneva a proposal (of Japanese origin) that a conference be set up at Shanghai, with neutral participation, to bring about a cessation of hostilities and the restoration of peaceful conditions on the basis that (a) Japan had no political or territorial designs at Shanghai, and (b) that the security and integrity of the International Settlement and French concession must be preserved. Japan and China accepted this proposal, the latter with the reservation that the conference would only be concerned with the restoration of peace at Shanghai, and that all

questions arising out of the Sino-Japanese conflict would be settled in accordance with the regular League procedure, and participation in the conference be subject to agreement regarding the agenda. On the 4th March, after the Chinese withdrawal, the Assembly of the League passed a resolution recommending that negotiations be entered into between Chinese and Japanese with the assistance of neutral representatives to render definite the cessation of hostilities and gulate the withdrawal of the Japanese forces.

- 105. In accordance with the above resolution a peace conference was constituted at Shanghai, in which the British, United States, French and Italian representatives assisted. The negotiations proceeded with the greatest difficulty, and were only kept from breaking down by the persistence of Sir Miles Lampson, the Chinese aiming at securing the complete withdrawal of the Japanese troops within the settlement within a fixed time, while the Japanese seemed determined to hold a temporary line dominating the Shanghai-Woosung Railway, "pending later arrangements," by which it was fairly clear that they intended arrangements for the demilitarisation of the Shanghai area. Finally, after all possible pressure had been put upon the Chinese to induce them to make the maximum concessions, the Japanese began to give indications of a desire to see the matter settled, possibly because they found it inconvenient to maintain a force of from three to four divisions in their line of occupation outside Shanghai, while reinforcements were urgently needed in Manchuria; and an agreement was signed on the 5th May, by which it was undertaken that the Chinese troops round Shanghai would "remain in their present positions pending later arrangements," and that the Japanese would withdraw temporarily to certain specified areas outside Shanghai, and thereafter to the settlement and extra-settlement roads where they had been stationed prior to the incident of the 28th January. A neutral commission was set up to watch the handing over and the preservation of order in the evacuated area, which was to be policed by special Chinese gendarmerie. The signature of the agreement was marred by the fact that Mr. Shigemitsu, the Japanese Minister, and General Uyeda, the chief Japanese military delegate, were lying in hospital suffering from injuries inflicted by a bomb thrown by a Korean during the celebration of the Japanese Emperor's birthday on the 29th April. The agreement has so far been observed on both sides with surprisingly little friction. The Japanese were apparently determined to liquidate their Shanghai venture, which had forced them unexpectedly to quite disproportionate efforts. The evacuation of the areas temporarily occupied under the terms of the agreement was completed by the 17th July, the withdrawal of the main Japanese forces from Shanghai having commenced as soon as the agreement was signed. One division was transferred immediately to Manchuria, where the activities of irregulars and bandits were causing considerable trouble to the Japanese military authorities.
- 106. An account of internal developments in Manchuria is given in the relevant section of the report (see paragraphs 66–76).
- 107. In July a dispute arose over the control of the customs at Dairen in connexion with the taking over of the Customs Administration in Manchuria by the new Government. The Japanese Government protested against the dismissal of the Japanese Commissioner of Customs, Mr. Fukumoto, which they alleged was a breach of the Dairen Customs Agreement of 1907, and refused to give their consent to the appointment of a new commissioner. The Chinese Government refuted this contention, and protested in turn against the action of the Japanese Government, who had allowed Mr. Fukumoto and his Japanese staff to usurp the functions of the Chinese Maritime Customs at Dairen on behalf of the Manchukuo Government. Mr. Fukumoto continued, however, to collect customs duties at Dairen.
- 108. The question of Japan's relations with the new State had been complicated by the necessity of maintaining her position on the Geneva front. Although the Manchurian Government was actually known to be a puppet of the Japanese Government, the Japanese outwardly maintained the pretence that it was the issue of a spontaneous independence movement, and at first maintained only de facto relations with the new authorities, protesting that the question of recognition must be decided on its merits later according to whether the movement

justified itself or not. Public opinion in Japan, however, pushed them towards recognition.

- On the 14th June the Diet passed a resolution in favour of speedy recognition of the new State. This provoked protests from the Chinese Government, both to the League and to the principal Washington Powers. An attempt was made by these Powers to persuade the Japanese Government to proceed with due caution in the light of their obligations under the Nine-Power Treaty to respect the territorial sovereignty and integrity of China, but the Japanese Government refused to admit that recognition would constitute a breach of this obligation and made known their determination to accord it in due course, although it was understood that this would not be until the League Commission of Enquiry, which was investigating the Sino-Japanese dispute, had left the Far East. Recognition was actually accorded on the 15th September (after the commission had left China, but before their report had reached Geneva). On this date General Muto, who had been appointed Commander-in-chief of the Japanese forces in Manchuria and concurrently Governor-General of Kwantung in order to unify the organs of Japanese administration in Manchuria, presented credentials as "Special Ambassador" to Manchuria, and signed a protocol regulating relations with the Changchun Government; the latter undertook to confirm and respect Japanese rights and interests in Manchuria, and both parties bound themselves to give each other mutual assistance in maintaining "national security," for which purpose Japan should station the necessary troops in Manchuria.
- 110. The Chinese Government at once lodged a protest in Tokyo, and at the same time protested to the League of Nations; they also addressed notes to the other Washington Powers alleging that the recognition of Manchuria constituted a breach of the Nine-Power Treaty and expressing the hope that measures would be taken to deal with the situation.
- 111. In October the Minister for Foreign Affairs of the Manchukuo Government, Mr. Hsieh Chieh-shih, paid a visit to Tokyo to thank the Japanese Government for having recognised the new State. The Japanese Embassy at Changchun was formally opened at the beginning of December.

(a) General.

(4) Russia.

- 112. There were constant rumours throughout the year that diplomatic relations between China and the Union of Soviet Socialist Republics were about to be resumed; these were for a time denied, but in June the Minister for Foreign Affairs admitted that the Chinese Government had in principle decided upon a resumption of relations. This question and that of negotiating a pact of nonaggression formed the subject of conversations which took place at the end of June in Moscow, between the Commissariat for Foreign Affairs and a member of the Chinese delegation under Mo Teh-hui, which originally went to Russia over two years ago to negotiate a settlement of the 1929 dispute. Negotiations were continued during the ensuing months, and on the arrival of the Soviet Commissar for Foreign Affairs, M. Litvinov, at Geneva in December, and simultaneously with the decision to invite Soviet participation in the League's deliberations over the Manchurian dispute, letters were exchanged on the 12th December between the principal Chinese delegate at Geneva, Dr. W. W. Yen, and M. Litvinov, under which their respective Governments undertook to resume relations.
- 113. It was subsequently announced that Dr. W. W. Yen would be proceeding to Moscow in the near future as Chinese Ambassador.
- 114. In May the Soviet Government agreed to the appointment of Manchukuo consuls to Vladivostok and other important towns in Eastern Siberia.
- 115. The question of communism in China is dealt with in paragraphs 47-49.

(b) Chinese Eastern Railway.

116. Of all Manchurian railways, the Chinese Eastern Railway suffered perhaps the most severely from the disturbed conditions which prevailed during 1932. The activities of anti-Japanese volunteers and of bandits first made themselves felt along the eastern section of the line, and by the month of March had

caused the virtual suspension of traffic between Harbin and Vladivostok. The other two sections were, save for a few sporadic attacks, left at first more or less undisturbed, but in the latter part of the summer conditions here too became chaotic as a result of disastrous floods and a marked increase in banditry. Communication between Harbin and Manchouli was often interrupted for weeks at a time, while even on the short Harbin-Changchun section trains were frequently railed or held up. Finally, with the rising in West Manchuria, which took prace late in September under General Su Ping-wen, the last semblance of an organised service on the western section disappeared, and by the autumn of 1932 it was only between Harbin and Changchun that trains were running with any degree of regularity, and even then only in the daytime.

117. It is at least possible that the Japanese do not regard the paralysis of the railway as an entirely unmixed evil. They look upon it as at once a serious competitor to the South Manchuria Railway, and the cornerstone of Soviet influence in North Manchuria, and they make little secret of the fact that they are determined eventually to render impossible its continued existence under its present administration. The new president of the railway, Mr. Li Shao-keng, and his colleagues have ever since the arrival of the Japanese in Harbin been faced with continual and often successful attempts to encroach upon the railway's rights and to limit its activities, while the ambitions and projects for railway construction recently formulated by the Manchukuo Government have as one of their principal aims the creation of a railway system which will render North Manchuria entirely independent of the Chinese Eastern Railway.

(5) United States of America.

- 118. On the 8th January the United States Government addressed a note to the Chinese and Japanese Governments simultaneously regarding the Manchurian situation; the note stated that the United States Government could not admit the legality of any situation de facto, nor did it intend to recognise any treaty or agreement entered into between China and Japan which might impair the treaty rights of the United States or its citizens in China, including those relating to the policy as regards China commonly known as the open door policy; and that it did not intend to recognise any situation, treaty or agreement which might be brought about by means contrary to the Covenant and obligations of the Pact of Paris.
- 119. Any hopes which might have been raised in China by this note were dashed again when the United States Government, in response to an enquiry from the Chinese Government as to whether the note presaged the calling of a conference of the Powers signatory of the Nine-Power Treaty, replied that they did not consider that such a conference would serve any useful purpose at the moment. The note therefore remained something of a paper gesture, although it did at least lay down the principle, later affirmed by the League resolution of the 11th March, of non-recognition of situations or agreements brought about in defiance of the Pact of Paris.
- 120. This was the only occasion during the year on which the United States Government failed to act, as regards the Manchurian question, in the closest concert with His Majesty's Government. During the Shanghai negotiations, for instance, and the crisis precipitated by the seizure of the Manchurian Customs, the loyal support and collaboration of the United States Legation was of the greatest assistance to His Majesty's Legation.
- 121. There were several cases during the year of United States citizens being captured by bandits and held to ransom. There was also in the summer a serious incident near Sianfu, when a party of four travellers, including an American resident of Hankow, were murdered in mysterious circumstances. This incident, which in several of its features bore a certain resemblance to the Thorburn case, formed the subject of protracted negotiations between the United States Government and the Waichiaopu, as a result of which it was announced at the end of the year that the officer responsible for the crime had been executed.

122. It is understood that on the 15th December ratifications were exchanged at Washington of the treaty of arbitration between the United States of America and China signed in June 1930 (see paragraph 230 of 1930 report) (see also Aviation).

(6) France.

- 123. The Haardt-Citroën expedition (see paragraph 179 of the 1931 report), travelling via Kansu and Mongolia, reached Peking from Sinkiang on the 12th February. They left a fortnight later by sea for Indo-China, whence it was their intention to start by car on the return journey through Siam, India and Persia to Beirut, whence the eastern section of the expedition had set out a year previously. The sudden death at Hong Kong, however, of M. G. M. Haardt, the leader of the expedition, caused the abandonment of these plans, and the expedition returned by sea to France from Saigon.
- 124. Earlier in the year the vexed question of the sovereignty of the Paracel Islands (see paragraph 180 of the 1931 report) was reopened, when the Kwangtung provincial authorities called for tenders for the exploitation of guano deposits on the islands. In consequence of this action the French Government addressed a note to the Chinese Legation in Paris setting forth the grounds upon which they held that the islands fell within the sovereignty of France and formulating reserves as to the future of the islands. As far as is known, the Chinese Government has not as yet replied to this note.
- 125. Towards the end of the year the Chinese Government approached the French Legation with a request for ratification of the convention concluded between China and French Indo-China on the 6th May, 1930 (see paragraph 232 of 1930 report). It is understood, however, that the French Government are reluctant to ratify the convention, considering that it accords too many concessions to the Chinese, without adequate quid pro quos on the French side.
- 126. The rumours which had been prevalent in the previous year regarding a secret understanding between France and Japan (see paragraph 182 of 1931 report) were again revived from time to time during 1932, and were categorically denied by the French authorities on more than one occasion.

(7) Germany.

- 127. In so far as Sino-German relations are concerned, there were no developments during 1932 worthy of record. Thanks in some measure to the presence in China of the German Military Mission, Germany was able during the year to secure a number of orders for war materials, military aeroplanes, &c.
- $128.\;$ A German missionary, Father K. Rapp, was murdered—apparently by Japanese soldiers—in the Chientao area of Manchuria on the 5th June.

(8) Treaties with Secondary Powers.

- 129. In view of the fact that the Sino-Brazilian Treaty of Amity and Commerce of 1881 was due shortly to expire, negotiations for the conclusion of a new treaty were begun at Nanking in October between the Brazilian Minister and the Waichiaopu. At the end of the year, however, little or no progress had been made, and it was understood that the Brazilian Legation had referred to Rio de Janeiro for further instructions.
- 130. According to a Kuomin news report of the 2nd August, negotiations were then in progress with the Chilean Government for the conclusion of a Sino-Chilean Treaty of Amity and Commerce.
- 131. By a National Government mandate of the 22nd July Ling Ping, Chinese Minister at Cuba, was appointed plenipotentiary delegate for the conclusion of a treaty of amity and commerce and navigation between China and the Republic of San Domingo.

- 132. In the latter part of the year negotiations were begun between the Waichiaopu and the Netherlands Legation with regard to the proposed remission of the Dutch share of the Boxer indemnity. Nothing had been formally concluded by the end of the year, but it was understood that a tentative draft agreement had been drawn up, under which, after certain debts owing by the Chinese to the Netherlands Government had been settled, 65 per cent. of the punds remitted would be devoted to conservancy work in China to be undertaken by Dutch firms, while the other 35 per cent. would be devoted to cultural purposes.
- 133. By a Government mandate of the 25th October Li Shih-chang, Chinese Chargé d'Affaires and consul-general in Panamá, was appointed plenipotentiary delegate to negotiate a treaty of amity, commerce and navigation with the Government of Panamá.
- 134. It was reported in the Chinese press towards the end of the year that negotiations with the Siamese Government were in progress which had as their ultimate object the conclusion of a commercial treaty between China and Siam. The treaty would be negotiated by the Chinese and Siamese Ministers in Tokyo. According to reports from His Majesty's Embassy, Tokyo, however, it appears that no negotiations have yet been opened.

(9) League of Nations.

- 135. The Sino-Japanese dispute has engaged the attention and activities of the League throughout the year. In September 1931, when the Japanese coup was carried out in Manchuria, China had appealed to the Council of the League under article 11 of the Covenant; and the Council's resolution of the 10th December, passed at the third meeting held to deal with the situation, had provided for the appointment of a commission to study the question on the spot.
- 136. When hostilities broke out at Shanghai on the 28th January, the Chinese Government lodged a fresh appeal invoking articles 10, 11 and 15 of the Covenant, and, on the 12th February, they requested that the dispute be referred to the Assembly. In the meantime, a special committee had been formed of the consular representatives at Shanghai of members of the Council other than Japan with the addition of the United States consul-general to report to the Council on the situation. For the Round Table Conference proposals (the so-called Boncour proposals) put forward by the President of the Council on the 29th February, see the section on the International Settlement at Shanghai.
- 137. A special meeting of the Assembly was held in March to consider the Chinese Government's appeal, at which, on the 4th March, a preliminary resolution was adopted calling for negotiations to render definite the cessation of hostilities at Shanghai, which had then just taken place. In a further resolution, on the 11th March, the Assembly dealt with the dispute more generally. The principle was laid down that it was incumbent on members of the League not to recognise any situation or agreement brought about by means contrary to the Covenant or the Pact of Paris; and a Special Committee of Nineteen was set up to handle the dispute, with power to convene full meetings of the Assembly as required.
- 138. On the 30th April a further meeting of the Assembly was convened, which took note of and approved the draft agreement for the cessation of hostilities prepared by the Shanghai Peace Conference.
- 139. Meanwhile, the Commission of Enquiry provided for by the Council's resolution of the 10th December had been appointed, with Lord Lytton (Great Britain) as chairman, and had proceeded to the Far East. The commission consisted of five members: United Kingdom, French, United States, German and Italian, with Chinese and Japanese assessors. They reached Japan on the 29th February, and, after a short visit, proceeded to Shanghai, where they arrived during the peace negotiations. The commission refrained, however, from taking any direct part in these negotiations. After visiting Nanking, Hankow and Peking, they proceeded to Manchuria in April, and submitted a preliminary report to the Council on the 30th April. (This report dealt with the existing military and political situation, and contained no comments or

recommendations.) After carrying out their investigations of the situation in Manchuria, the commission returned to Peking, where they remained, but for another short visit to Japan, during the preparation of their final report, which was completed and signed on the 4th September. The report reached Geneva on the 22nd September, but the Council, which met on the 24th September, decided, at the request of the Japanese Government, to postpone discussion of it until November. (A special resolution had already been passed extending the period of six months within which, according to article 15 of the Covenant, the Assembly was bound to pronounce on the dispute, in order to give time for the consideration of the commission's report.)

140. The first meeting of the Council to consider the report took place on the 21st November. The Japanese delegation, before the meeting, had circulated to the members of the Council a memorandum criticising certain portions of the report, and the members of the commission, who had been invited to attend the session of the Council, were asked whether, in the light of this memorandum, they desired to modify the report. This reply being in the negative, a resolution was passed affirming that the report furnished a basis for settlement, and, despite strenuous opposition from the Japanese delegation, the matter was, on the 28th November, referred to the Assembly. After protracted deliberations by that body, it was suggested by the United Kingdom delegate that the Committee of Nineteen should be reconstituted and reinforced by the inclusion of representatives of the United States of America and the Union of Soviet Socialist Republics, for the purpose of evolving a definite plan of conciliation. This proposal was adopted by the Assembly, but, at the end of the year, neither the United States of America nor the Union of Soviet Socialist Republics had definitely signified their willingness to participate in the committee's deliberations.

141. The tendency to enlist the advice of the technical services of the League, remarked on in the report for 1931, has not been continued during the past year. China has been too much preoccupied by the conflict with Japan and the resulting Government crises, which have undermined such political stability as she had previously attained, to devote serious attention to schemes of social and economic reconstruction. General interest has been focussed on the League by the submission to it of the Sino-Japanese dispute, and the orientation of China in favour of or against further co-operation in the immediate future will probably depend to a large extent on the way in which the question is handled at Geneva, and on the success or failure of the League in achieving a solution.

(10) International Settlement at Shanghai.

142. The problems connected with the settlement have, like other questions in China, been influenced, and to a large extent dominated, by the Sino-Japanese dispute, and particularly by the hostilities which took place at Shanghai in January and February (of which an account is given elsewhere).

(a) Defence of Settlement.

143. In November 1931 the municipal council became concerned over the possibility of a state of war breaking out between China and Japan, and an informal meeting of the Defence Committee was held to discuss the problem of preserving order in the settlement in that event. The foreign commandants then informed the chairman of the council that, upon the declaration of a state of emergency by the council, they were prepared to act in accordance with the defence scheme, which was already in existence. A state of emergency was actually declared on the 28th January, following the presentation by the Japanese authorities of their ultimatum to the Mayor of Shanghai, and the defence scheme was thereupon brought into force. This scheme envisaged the occupation by the various foreign forces of a defence line, embracing not only the settlement itself, but also certain areas surrounding the council's extrasettlement roads in the western and northern districts. In particular, the sector assigned to the Japanese forces included an area in the Hongkew district thickly populated by Chinese and Japanese, and bordering on the Chinese controlled districts of Chapei and Paoshan. It was this which, as described

in the section on Sino-Japanese relations, enabled the Japanese authorities to maintain that the original clash between their troops and the Chinese was merely the result of their attempt to occupy the positions assigned to them in the scheme. This circumstance illustrated a serious danger inherent in the defence scheme, but it is difficult to see how it could have been avoided.

- It was feared at first that the foreign Powers generally might be involved in the clash through attacks on the settlement by the Chinese troops. In fact, however, the foreign forces other than the Japanese were able to observe strict neutrality throughout. The attitude of the Chinese troops at the points where their positions were adjacent to those of the foreign defence forces was friendly, and they were on the whole careful to respect the neutrality of the settlement. One or two cases only occurred of the bombardment of the wharves and water-front of the settlement behind the Japanese lines by Chinese guns, against which protests were lodged by the Powers. The Chinese Government, on their side, protested against the use of the settlement by the Japanese as a base of operations, and the landing of troops and stores there to support the Japanese attack. His Majesty's Government caused representations to be made to the Japanese Government deprecating the use of the settlement as a base of operations unconnected with the defence of the settlement, and the United States, French and Italian Governments made more or less similar communications. In addition, protests were lodged on several occasions by His Majesty's Minister and his colleagues with the Japanese authorities in Shanghai. These were not altogether without effect, as the majority of the later Japanese reinforcements were landed outside the settlement. Military and naval reinforcements were hurried to Shanghai by all of the four Powers mentioned above for the protection of the settlement (and the French concession), His Majesty's Government sending three cruisers and augmenting the land forces to a strength of four battalions of troops.
- 145. The technical state of emergency was maintained in the International Settlement until the 13th June.
- (b) Proposal of a Round Table Conference.
- 146. In February, while hostilities at Shanghai were still in progress, the Japanese delegate at Geneva informed certain members of the Council that it was Japan's intention to attempt to secure a solution of the Shanghai question in concert with the other interested Powers, and that for this purpose she was prepared to hold a Round Table Conference at Shanghai, with a view particularly to arrangements for the safeguarding in future of foreign residents. (In this connexion the tentative proposal published in Tokyo earlier in the month for the establishment of demilitarised zones at Shanghai and elsewhere in China an indication of the nature of the arrangements which Japan had in mind.) suggestion was taken up and embodied in a proposal put forward by the President of the Council on the 29th February for the immediate setting up of a conference at Shanghai, consisting of representatives of China and Japan and the principal Powers having special interests in the Shanghai settlements, to bring about "the restoration of peaceful conditions in the Shanghai area," the conference to be undertaken on the basis that Japan had no political or territorial designs at Shanghai, and that China recognised the necessity of preserving the safety and integrity of the settlements. The proposal was accepted by the Powers concerned, but by China with the reservation that the conference should only be concerned with the restoration of peace, and that participation in it would be conditional on agreement as to the agenda.
- 147. The cessation of hostilities, which took place upon the retirement of the Chinese troops from the neighbourhood of the International Settlement on the 3rd March, was followed by peace negotiations with neutral participation in accordance with the League Assembly's resolution of the 4th March and the conclusion of the agreement of the 5th May, which provided for the withdrawal of the Japanese troops, removed, in the Chinese view, the need for any further conference. The resolution of the 4th March had, however, been expressly stated to be without prejudice to the suggestions previously made by the Council, and the Japanese still looked forward to the holding of a Round Table Conference, and had succeeded in inserting in the agreement a provision that the Chinese troops should remain in their existing positions (i.e., should not approach nearer to the

settlement) "pending later arrangements." His Majesty's Government, for their part, in common with the United States Government, would have been glad to see the Round Table Conference proposals dropped once peace had been restored at Shanghai. They were doubtful of the possibility of reaching any agreement with China on the Shanghai question at a conference called in the existing circumstances, and were also unwilling to be associated with any attempt by Japan to extort concessions under the threat of military force.

- 148. On the 13th May the Japanese Minister for Foreign Affairs approached the United Kingdom, French, United States and Italian representatives at Tokyo, and informed them that the Japanese Government attached great importance to the holding of a Round Table Conference. He suggested preliminary conversations at Tokyo without the Chinese, with a view, if possible, to reaching agreement on the lines which the conference should follow. After consulting together, the Powers concerned replied (on the suggestion of His Majesty's Government), pointing out that anything like a preliminary conference at Tokyo would merely arouse the suspicions of the Chinese and intensify their opposition to the Round Table Conference, and suggesting that, instead, the Japanese Government should instruct their representatives at the various capitals to develop their ideas on the subject to the Powers concerned. (It was held impolitic to reject the Japanese proposal outright, for fear of giving Japan an excuse to take independent action.)
- 149. The foreign community in Shanghai in general has expressed itself strongly in favour of the Round Table Conference. When the first indignation caused by the high-handed action of the Japanese had died down, a vocal body of opinion began to urge that the opportunity should be taken to force a settlement of outstanding issues with the Chinese with the assistance of Japan.
- 150. This view was put forward to His Majesty's Minister by the Joint Committee of the China Association and the British Chamber of Commerce, and, at his request, was later embodied in a memorandum, in which the main questions calling for a solution were stated to be: (1) The inefficiency of the special district court; (2) the administration of the extra-settlement roads; and (3) the danger arising from the presence of large bodies of Chinese troops in the vicinity of Shanghai. It was urged that the solution of these questions should form part of the final settlement of the Sino-Japanese differences, and that the United Kingdom Government should take part in bringing about such a settlement.
- 151. On the 31st May the Shanghai General Chamber of Commerce forwarded to the senior consul, for communication to the Diplomatic Body, a resolution requesting the Powers to convene a Round Table Conference as soon as possible to deal with the above questions and expressing the view that the municipal authorities of the International Settlement and the French concession should be represented at the conference. No joint action was taken by the Diplomatic Body on this resolution.

(c) Extra-Settlement Roads.

152. In March, while the peace negotiations were in progress at Shanghai, His Majesty's Minister took the opportunity to urge upon the mayor and the Vice-Minister for Foreign Affairs that it was in the interests of the Chinese Government to bring about an amicable solution of the various points of friction between the settlement and the Chinese authorities. He alluded in this communication to the drive in many quarters for measures to be taken to protect the interests of the foreign settlements. As a result of this and similar promptings, as well as of advice given by His Majesty's consul-general to the municipal council, conversations were reopened between the Chinese Municipality and the council on the outside roads question, and a draft agreement was initialled on the 4th June by which the policing of these roads was to be handed over to a special body of police under the control of the Chinese Municipality, but with a deputy commissioner appointed by the municipal council of the settlement, who would handle all matters concerning foreigners, orders relating to such matters requiring his counter-signature; in return, the Chinese Municipality would delegate to the settlement authorities the power to maintain the roads and the health and fire-prevention services, together with the right to collect taxes in the extra-settlement roads area (any surplus to be divided equally between the

Chinese and foreign municipalities). The draft was referred to the Chinese Government and, after some modifications and discussions, was transmitted by the council to the consular body for comment at the end of July. In the meantime it had become evident that the Japanese were likely to oppose the agreement, partly because they objected in particular to the policing of the northern extrasettlement area, which contains many Japanese residents, by the new Chinese police, and partly because they desired, in any case, that all such questions should be reserved for the proposed Round Table Conference. In order to avoid giving occasion for official controversy over the matter, the British and United States authorities had taken the line that the conclusion of the agreement was a matter of the council's internal administration and did not require the consent of the consular body under the Land Regulations. It was hoped that the agreement might thus be concluded with the minimum of fuss and the Japanese given no opportunity to obstruct it. When the draft was communicated to the consular body, however, the Japanese consul-general at once raised objections, and when the signature of the agreement in the face of Japanese opposition was proposed, the Japanese councillors threatened to resign. On the other side, the Chinese authorities began to weaken and refused to allow the publication of the agreement before signature, to which the foreign councillors felt themselves committed. A suggestion that the arrangement as a first step should be put into force in the western district only (where Japanese interests are negligible as compared with British) was rejected by the Chinese as being an admission that the Japanese had some special rights in the northern district, and it was finally agreed that it was useless to proceed with the agreement for the moment, and that its conclusion must await more favourable conditions.

Discussions with a view to finding a means of overcoming Japanese objections to the draft agreement in its present form took place in the latter part of the year between His Majesty's consul-general and the newly-appointed Japanese consul-general, Mr. Ishii, as a result of which it became clear that, while most of the obstacles placed by the Japanese in the way of acceptance of the draft were not insurmountable, the question of the foreign personnel in the proposed special police force was the real stumbling-block. The Japanese were determined that this force should be virtually in Japanese control, and insisted that as a condition of their accepting the draft, it should be agreed that not only should the foreign Deputy Commissioner be a national of that country having the largest number of residents on the outside roads (i.e., Japan), but that most of the other principal positions in the new force should be filled by Japanese. Sir John Brenan, while admitting that the Japanese, in view of their numerical superiority among the foreign population of Shanghai, had a legitimate claim to a large measure of participation in the constitution of the proposed new police, nevertheless intimated that His Majesty's Government would be unlikely to accept any arrangement which ignored our preponderating financial interest in Shanghai and the leading part which British capital and British enterprise had played in the development of the port. Mr. Ishii promised to refer the matter to Tokyo for further instructions, and at the end of the year the whole question was still under consideration.

(d) Chinese Courts in the Settlement.

154. During the Sino-Japanese hostilities at Shanghai a wave of foreign criticism arose against the special district court. It was pointed out that the subservience of the Chinese judges to political influences had been clearly shown in connexion with the anti-Japanese boycott, and it was alleged that the impossibility of obtaining redress in the courts against the illegal activities of the boycott organisations had been one of the factors which had compelled the Japanese to resort to drastic action. At the same time attention was called to the deficiencies of the courts as a means of enforcing civil contracts (principally owing to the delays in procedure and the difficulty of getting judgments executed). The foreign community at Shanghai clearly hoped that advantage might be taken of the Japanese military pressure on China to impose a modification of the system, and the idea of an international court with foreign judges was put forward.

155. The revision of the Shanghai Court Agreement of the 17th February, 1930, was one of the points proposed by the Shanghai Chamber of Commerce for

consideration by a Round Table Conference in their resolution of the 31st May (see above).

- 156. The United Kingdom and United States Governments, after consulting in the matter, were agreed that there was nothing to be gained by opening negotiations for the revision of the court agreement (which is due to expire on the 31st March, 1933), but rather that it was desirable, if possible, to obtain the renewal of it in its existing form. It was, in any case, clearly impossible to eliminate political influence from a Chinese court by the terms of an agreement, and, in the light of the 1930 negotiations, it was certain that no Chinese Government could be got to consent to the establishment of an international court; Chinese propaganda was, on the contrary, urging the abolition of the existing safeguards of foreign interests embodied in the agreement when the latter should come up for revision.
- 157. It was therefore decided to impress upon the Chinese Government the force of the foreign criticisms of the court, which would have to be taken into account if the question were reopened, and to urge that in the interests of all concerned the agreement should be renewed in its present form and attempts in the meantime made to improve its efficiency and to remove causes of criticism by friendly adjustment. His Majesty's Chargé d'Affaires broached the matter to the Minister for Foreign Affairs during his visit to Nanking in October, and made tentative proposals along the above lines. Dr. Lo welcomed the proposal but explained that, pending receipt of the report of a committee of representatives of the Waichiaopu and the Ministry of Justice which had been set up to consider the whole question, he was unable to come to any decision. In the course of an interview on the 15th December, however, he gave Mr. Ingram a verbal assurance that he was prepared to prolong the agreement rather than revise it. At the end of the year arrangements were being considered for the signing by the interested parties of an instrument formally recording the prolongation of the agreement.

(e) Judge Feetham's Report.

158. The fourth and last volume of Judge Feetham's report, dealing with details of the administration of the International Settlement, was submitted to the municipal council in January 1932, and was published during the summer.

III.—RAILWAYS.

159. Though not subjected to the operations of large-scale civil wars, the past year has not been an altogether happy or prosperous one for the Chinese railways, and there is little development or new construction to record, while the arrears of debt are steadily accumulating. The Shanghai-Nanking Railway was almost completely put out of action for normal passenger and freight services for some weeks during the Sino-Japanese struggle around Shanghai, which began at the end of January. Through traffic on the line was not resumed till the 24th May, the day after the Japanese had handed the Shanghai end of the line back to the Chinese, while through traffic on the Shanghai-Hangchow-Ningpo line was resumed a day or two later. The two railways suffered damage to their properties as the result of these hostilities, to the extent of nearly 17 million dollars, the principal item being one of 10 million dollars to cover the replacement cost of the plant and machinery at the Woosung workshops.* The Peking-Hankow line was for some months of the year in the centre of activities between the Government anti-Communist forces and the Red armies in Hupeh and Honan, and was frequently subject to severe bandit raids, which seriously interfered with traffic; the same may be said of the Lung-Hai Railway and the Wuchang-Changsha section of the Canton-Hankow line. The Peking-Mukden Railway has been throughout the year divided into two sections at Shanhaikuan, the northern portion of the line (now known as the Fengshan Railway), being controlled by the Manchukuo authorities under a separate administration at Mukden. All efforts to negotiate the restoration of through traffic between Mukden and Peking failed, and no trains from either direction are allowed to

^{*} It was later stated that "the damage at Woosung had turned out to be less than was expected."

pass through Shanhaikuan. Generally speaking, the state of the rolling-stock and permanent way on the main railway systems of China is deplorable (though this defect is to some extent being met out of grants from the British indemnity funds), and very large sums will be needed to put them in an efficient condition.

Financial Position.

160. A statement of the financial position of the railways, in which the British and Chinese Corporation and the Chinese Central Railways (Limited) are interested—in other words, all the Chinese railways in which there is a substantial British interest—shows that at the 30th June, 1932, repayments of principal were in default to the extent of £5,607,835, and of interest to the extent of £4,049,466. The total amount of the original loans was £23,442,761, of which £17,616,587 is still outstanding, including the repayments in default abovementioned.

Railway Legislation.

161. A large volume of legislation has been promulgated by the Nanking Government during the past year, possibly to forestall criticisms in the League of Nations report on Manchuria, including a new Railway Law (see also under Legislation). The main object of all this legislation is to increase the authority of the Central Government—in many cases still almost entirely lacking—over the railway administrations, and a special law provides for the management of the various railways being placed in the hands of committees, consisting of a chairman and four members, all of whom are to be appointed by the Minister of Railways. It seems unlikely, however, that it will be possible for some time to put this law into practice, except on the railways whose administration is directly controlled from Nanking (e.g., the Tientsin—Pukow line, where such a committee is already functioning)—see also under Peking—Mukden and Peking—Suiyuan Railways.

Shanghai-Nanking Railway.

162. Since the destruction of the Shanghai north station, the terminus of the Shanghai–Nanking and Shanghai–Hangchow–Ningpo Railways, during the Sino-Japanese hostilities early in the year, plans have been made to sell the land at the old station and build a new one at Chenju, 5 miles west of the present station, at a cost of some 10 million dollars. The British and Chinese Corporation have had to object to this extravagant project as decreasing the bondholders' security, and in view of the fact that the railway are now indebted to them to the extent of some 12 million dollars. Opposition has also been evinced by the landowners in the district concerned, who will be expropriated if the scheme goes through, probably without any prospect of payment for their land. A plan for the taking over of the Woosung branch line by the City Government of Greater Shanghai was mooted in August last, to which the corporation would also be forced to object under the terms of the Shanghai–Nanking Railway Loan Agreement of 1903. All these schemes are really part of the Chinese plan for the establishment of a new civic centre at Shanghai, the development of the Woosung area, and the provision of greater railway facilities in connexion therewith.

Shanghai-Hangchow-Ningpo Railway.

163. The Ministry of Railways recently approached the British and Chinese Corporation for a loan for 10 million dollars for the completion of the railway between Hangchow and Ningpo, and the implementation of the Nanking-Hunan Railway Agreement.

Shansi Railway.

164. The Chengting-Taiyuanfu (Shansi) Railway, built with French capital in 1902, was formally "taken over" by the Chinese Government on the 25th October, 1932, after the expiry on the 15th October of the loan agreement, the financial arrangements for the redemption of the line, apart from certain minor details, having been satisfactorily arranged. In July a draft contract was signed between the French engineer-in-chief of this line, Mr. Martin, with the Vice-Minister of Railways, for a loan to construct a railway—a project frequently

mentioned previously—between Shihchiachuang, the eastern terminus of the Shansi Railway, and Tsangchow on the Tientsin-Pukow line, to be continued thence to Taku at the mouth of the Hai Ho near Tientsin. Such a line would link up the Tientsin-Pukow, Peking-Hankow and Shansi Railways. The building of this line might be held to affect the rights of the Peking-Mukden (Peiping-Liaoning) Railway, if it were extended to Taku. The construction of a railway from Tatung to Tungkuan, from north to south of Shansi, connecting the Peking-Suiyuan, Chengting-Taiyuanfu, and Lung-Hai Railways is also spoken of.

Lung-Hai Railway.

165. At the western end of the railway the line has now reached within $2\ li$ of the Shensi border. The station at Tungkuan was opened to traffic on the 1st October. The road bed and bridge abutments have been completed as far as Hwayingmiao, $45\ li$ west of Tungkuan, but it is understood that further work is held up for lack of funds. The survey has been completed to Sianfu, $280\ li$ west of Tungkuan, and it is thought that once work is begun the line can be completed in eighteen months. Work is proceeding on the extension of the line from the eastern terminus at Haichow towards Hsuchow on the coast, now considered as the final terminus, where the construction of a new deep-water harbour has been talked of, though no work has actually been commenced and the scheme may be abandoned. The eastern end of the line from Hsuchowfu (the junction with the Tientsin–Pukow Railway) to Tapu (Haichow) is in very bad condition with poor material.

Kiao-Tsi (Shantung) Railway.

166. Attracted by the present low value of the Japanese yen, the Chinese Government have recently had under consideration the question of redeeming the railway by paying the Japanese Government the 40 million gold yen (now equivalent to about 32 million dollars) accepted as the valuation of the railway properties in the detailed agreement signed at Peking in December 1922 as the result of the general agreement for the transfer of the line negotiated at the Washington Conference. The Treasury notes handed to Japan in accordance with this agreement bore interest at 6 per cent. per annum, and redemption of the line could be effected at any time five years after their delivery on giving six months' notice, the full term of their currency being fifteen years; funds for the purpose could not, however, be raised from any but a Chinese source. The amount owing to Japan is now understood to have been increased by several years' arrears of interest, so that it is probably in the neighbourhood of 50 million yen. The earnings of the line are said to amount to about 5 million dollars a year. A bond issue, sufficient for redemption, in China at the present time is hardly practicable, and the cost of such a loan to the State would probably be very much greater than the 6 per cent. now payable to the Japanese.

Peking-Suiyuan Railway.

167. The chief personal aide-de-camp of Marshal Chang Hsueh-liang, General T'ang Kuo-chen, was in December appointed to the post of Director-General of the Peking-Suiyuan Railway. The appointment was made by the recently-established Peiping Political Affairs Committee. At the same time it was reported that the Ministry of Railways had nominated a committee (see paragraph 243) to manage the line, of which General T'ang was a member. This report is now denied, but it seems probable that the young marshal objected to the action of the Ministry of Railways, and that the instruction was in consequence withdrawn.

Hangchow-Kiangshan (Chekiang) Railway.

168. The first section of this light (standard-gauge) railway was opened from Hangchow to Chuki in 1931; the second section, from Chuki to Kinhwa, in February 1932; and the third section, from Kinhwa to Lanchi (200 kilom. from Hangchow), in March 1932; the line is eventually to be continued to Kiangshan, towards the Kiangsi border, and possibly to Yushan in Kiangsi. The locomotives were acquired from Germany and the rest of the rolling-stock from the United States of America (a grant of £200,000 for the completion of the line hitherto

built with Chinese money has now been obtained from British indemnity funds (see paragraph 223); the consulting engineer of the railway is an American citizen.

Peking-Mukden Railway.

- 169. Payment of the monthly service (about £7,000) of the original loan of 898 for the construction of the Peking-Mukden Railway and of the instalment of £10,000 a month towards the liquidation of the much overdue arrears of payment of the Double Track Loan of 1921 has throughout the year continued to be made by the Mukden authorities, out of moneys standing to the credit of the Railway Administration in the Chinese banks at Mukden before September 1931 (see paragraph 202 of last year's report). The British and Chinese Corporation have had very great difficulty in obtaining the additional monthly contribution of 10,000 dollars, originally promised in September 1930, from the director-general of the railway at Tientsin, although the surplus revenues of the railway were accumulating to the tune of several millions of dollars in the Chinese banks at the latter place. Finally, a dispute arose over these funds between Marshal Chang Hsueh-liang and Wang Ching-wei. The former is said to have asked the latter for 2 million dollars to pay for some ammunition lying at Tongku. This request was refused, whereupon the marshal said he would take it from the railway's surplus, accounting for every dollar spent. Wang Ching-wei demanded that, if the railway paid this sum to the marshal, a similar amount should be remitted to the Ministry of Railways for the payment of the obligations of the line, but he refused to state what obligations. A deadlock ensued, resulting in the resignation of both parties (see paragraph 14), and in the meantime the marshal ordered the director-general of the railway to pay him 500,000 dollars, while he collected the balance required from other sources.
- 170. After a protest had been lodged by the British and Chinese Corporation against this payment, the Ministry of Railways retaliated by ordering the railway in October to hand over 4 million dollars lying on deposit to the corporation to pay off the whole of the outstanding balance of the Double Track Loan (about £155,000), the remainder to be used for payment of the arrears of amortisation of the Shanghai–Hangchow–Ningpo Railway (£75,000). The director-general of the railway treated the order as not seriously meant, and, in spite of strong pressure brought to bear on the marshal by this Legation, the best offer that could be obtained from the director-general was that, if the corporation continued to collect the monthly instalment of £10,000 from Mukden for the next ten months, the Tientsin office would pay off the balance of the loan (£50,000 odd) in the same period, i.e., at the rate of some £5,000 a month. The only good point about the offer was that it constituted a definite undertaking, while the previous offer made in September 1930 was considered by the director-general to be of a provisional nature. The first instalment of £5,450, including accruing interest payable under this scheme, was paid at the end of November. Although there was some delay in payment, the November and December instalments of the two loans, as above stated, were finally remitted from Mukden in the latter half of November.

Canton-Hankow Railway.

171. It is expected that the Shuikwan–Lokcheong (Kwangtung) section of the line will be completed in six months, some 7 million dollars having already been spent on the work (see also paragraphs 223 and 224).

Canton-Kowloon Railway.

172. Services on this railway have been considerably accelerated during the past year, and it is expected that the journey from Canton to Hong Kong will be reduced to three hours and seven minutes.

Tientsin-Pukow Railway.

173. In drawing the attention of the Chinese Government to the accumulating defaults in payment of the loan services on this line, His Majesty's Government have persistently impressed upon the Chinese Government their obligation, under articles 9 of the Loan Agreement of 1908 and the supplementary agreement of 1910, now that *li-kin* has been abolished, to substitute an

equivalent security on the customs revenues. This request has, however, up till now been ignored, and it is understood that the Minister of Finance is firmly opposed to the customs revenues being used as security for this or any other railway loan. Similar representations have been made jointly by the American, French and British Legations in regard to the corresponding clause in the Hukuang Railways Loan Agreement of 1911, but equally without result.

- 174. The Ministry of Railways undertook to set aside every monthybeginning with August 1932, a sum of from 50,000 to 100,000 dollars, to be deposited in a special fund in the Bank of China at Nanking, to meet payments due on this railway's loans; the monthly payment was to be increased by 40,000 dollars from October onwards, thereby raising the amounts set aside each month to between 90,000 and 140,000 dollars. It was understood that as soon as these deposits reached an appreciable amount the repayment of principal and interest would commence.
- 175. The Chinese Government remitted funds from these deposits in December to meet the German portion of the loan of 1908, coupon 33, due on the 1st October, 1924, this being the first payment made by the Chinese Government on either the British or the German portion of the construction loans since 1926. As has been pointed out, however, by the British and Chinese Corporation to the Ministry of Railways, the monthly instalments deposited for loan payments will have to be increased many times to have any material effect in reducing the very large arrears of amortisation of the loan services now in default. The corporation hopes to make similar arrangements with other railways, whose loans are in default, such as the Shanghai–Nanking and Shanghai–Hangchow–Ningpo Railways.

Railway Freight Discrimination.

- 176. Constant representations made by Sir Miles Lampson, both written and personal, to the National Government in regard to discrimination against foreign interests in the matter of railway freights (see paragraph 204 of last year's report), as embodied in the freight schedule issued by the Ministry of Railways in June 1931, finally resulted in an order made effective as from the 1st January, 1932, but not immediately put into practice, abolishing the discriminatory rates on cigarettes complained of by the British-American Tobacco Company (Limited). This order maintained, however, the objectionable (in the case of cigarettes) principle of freight assessment in accordance with the value of goods carried. The above-mentioned company are left with a claim against the Chinese Government for excess freight payments arising out of schedule complained of amounting to 63,813-67 dollars, and instructions have been sought as to whether this unusual form of claim should be presented through His Majesty's Legation.
- 177. Discriminatory railway freight rates in the form of a special rebate granted to a Chinese oil concern on the Shanghai-Nanking Railway were cancelled in December on representations made by Mr. Ingram to the Minister of Finance.
- 178. A further instance of internal discrimination against foreign firms which may be mentioned here is apparent in the treatment afforded to the General Forge Products (1929) (Limited), a British company established in Shanghai to operate a factory making nails, bolts, &c., chiefly for use in shipbuilding works. In spite of the continued handicap of the so-called interport duty (equivalent to a full export duty), from which all industries in China still suffer, the factory had established a market in this country for its products in competition with imports from abroad, till, in 1930, a smaller Chinese nail factory was set up in Shanghai, organised by a man who had been trained in the British factory, and who took with him skilled operatives from the latter factory. The British firm discovered some months ago that this Chinese concern had been granted preferential exemption from payment of all customs duties for a period of three years "as the reward for first invention," though there was no sort of invention incorporated in its products. The case was taken up strongly with the Chinese Government, as being contrary to international precedent and a deliberate discouragement to the investment of foreign capital in China, and His Majesty's Chargé d'Affaires mentioned it to the Minister of Finance,

Dr. Soong was understood to be opposed to the discrimination practised in this case, but found it difficult to deal with, since the privilege, as in other similar cases, had been granted by his brother-in-law, the Minister of Industry. At the end of the year the Chinese Government had still taken no action to remove the discrimination.

179. The questions of the railway material debts (see paragraph 211 of last ear's report), and of the claims of British ex-employees of the Chinese Government railways (see paragraph 205 *ibid*), are dealt with in this report in paragraph 263.

180. The Manchurian railways are dealt with under the heading of Manchuria (see also paragraphs 116–117).

IV.—FINANCE AND TAXATION.

• 181. It will be recollected that, on the 19th December, 1931, Dr. T. V. Soong, the Minister of Finance, tendered his resignation as the result of the changes in the Government at that time. It was clearly a case of "reculer pour mieux sauter," for the financial position of the country could hardly have been worse, and Dr. Soong, in addition, contrived to leave an empty exchequer for his successors. The expected quickly happened, for, on the 29th January, he was reappointed. He did not, however, come back to any kind of a bed of roses. At a moment when the nation's finances were in a critical condition, the revenues decreasing, and the Government's internal bonds slumping heavily, the struggle with the Japanese round Shanghai in February was about to reduce the financial and commercial centre of the country to a state of utter stagnation for some weeks. The story of the remarkable way in which the situation has since been retrieved during the past year is told by Dr. Soong, more graphically than anyone else could tell it, in a statement made to the third plenary session of the Central Executive Committee of the Kuomintang, held at Nanking in the month of December. This statement is an epitome of the aims and progress of the National Government in matters of financial administration, as well as of its failures and weaknesses; to read it, and to read between its lines, is to get a grasp of the whole picture. Attached to Dr. Soong's statement are figures of the national budget for the two financial years, ending respectively at the 30th June, 1931, and the 30th June, 1932. Dr. Soong claims that, for the first time in the twenty-one years of the republic, the Chinese Government has been able to produce a properly balanced budget, and that, at a time of world-wide economic depression, and for the last few months at any rate (since January 1932), without recourse to borrowing.

182. The difficulties of the task are easily realised. Following upon the disasters of the previous year—trade depression, the slump in silver, the Manchurian crisis, the Yangtze floods—the Chinese Government has in 1932 had to face such additional difficulties as the resistance to the Japanese around Shanghai, flood relief on a huge scale, the anti-Red campaign, and the non-remittance of the Manchurian customs and salt revenues. It is only by means of the most stringent retrenchment, particularly as regards the salaries of Government servants—as Dr. Soong says: "The Government has been stripped of everything not necessary to its existence"—by improvement in tax administration, and, above all, by conversion of the internal loans, that the balancing of the budget has been made possible.

183. After the new Government had in January threatened to declare a moratorium on the domestic loan issues, and the Shanghai bankers had promised to advance a sum of 8 million dollars to tide them over the New Year, Dr. Soong inaugurated his return to office by making a bargain with the bankers, by which it was agreed that interest on all domestic bonds should be reduced to a par rate of 6 per cent., and the period of amortisation roughly doubled, the whole of these loans being henceforth secured on the surplus customs revenues only (an arrangement by which, it may be remarked, the Inspector-General of Customs has become more than ever the trustee for the internal bondholders). The economy to the Government in debt charges effected in this manner is placed by Dr. Soong himself as high as 100 million dollars a year. To appease the bankers, who must have

suffered heavy losses through this arrangement, the Government undertook (possibly making a virtue of necessity) not to contract further loans from commercial institutions to finance civil war or to cover the administrative expenses of the Government, while it guaranteed that the sinking fund, supplied from the surplus customs revenues, earmarked for the maintenance of the domestic bond credit, should never be used for any other purpose than that for which it was established. It is a remarkable fact, and one which testifies to the public confidence in the Customs Administration, that, since this scheme was put into force, internal bonds have been sold, towards the end of the year, at prices 40 per cent. higher than before conversion. The considerable rise in the price of several Chinese bonds on the London market also testifies to the confidence felt abroad in the future of the country in spite of its political difficulties.

184. Following on these internal loan conversion arrangements, Dr. Soong again tendered his resignation in June. This time the resignation did not take effect, and it was probably intended, as he himself phrased it, as a bombshell to make the people realise the imperative need for retrenchment and for the abandonment of civil war. It had, indeed, become clear that the Government must steer clear of all internal disputes if it was to continue in existence at all, and this policy has no doubt dictated the "forbearance" with which, as its spokesmen pride themselves, the Government have refrained from interference in the recent civil wars in Shantung and Szechuan.

185. The other reform in which Dr. Soong takes pride is the simplification of the tax system under three collecting agencies—the Customs, the Salt Gabelle Into the last of these the Wine. and the Internal Revenue Administration. Tobacco and Stamp Tax and the Consolidated Tax Administrations have been welded, so that China now possesses a "simple, unified and relatively logical system of national taxation." Dr. Soong points out that conditions in China are Dr. Soong points out that conditions in China are such as almost entirely to preclude the employment of direct taxation. His aim has been, therefore, to concentrate on the improvement of indirect taxation along the following lines: (1) Reduction of the number of taxes; (2) enforcement of uniform rates; (3) abolition of duplicate taxation; (4) consolidation of the tax organs into three administrations; (5) elimination of unnecessary personnel; and (6) the adoption of a civil service system to give officials the benefit of regular pay, security of tenure, and promotion according to merit. It is interesting to compare this statement of desiderata with the actual state of taxation throughout the While no doubt considerable reforms have been accomplished and much corruption and duplication weeded out in the Ministry of Finance itself, the authority of the Government over the provinces in matters of taxation is still woefully lacking, and there is still a long way to go before financial unification can be accomplished. In spite of Dr. Soong's remarks about the unsuitability of direct taxation, spasmodic efforts have been made during the year to introduce the business tax throughout the country, particularly at Hankow, even to the extent of refusing a hearing in the courts to plaintiff foreign firms which have not paid the tax. The method of collection of this tax is, moreover, in many respects directly opposed to Dr. Soong's statement of the reforms his Ministry seeks to inaugurate. There is, for instance, little or no uniformity about the tax, for each province is at liberty to assess the rates at which it is collected on various trades, while at Hankow it has even been farmed out in the pernicious manner of former years. In spite of the praiseworthy and sincere efforts of the Government to wipe out other internal taxes of the nature of the former li-kin, it has to be admitted that in the areas under their control, the semi-independent militarists still collect any taxes they please under various high-sounding titles on goods produced or in transit, even in the provinces close to the capital; with every transfer of military power, the tax collectors change also, with the result that there is no regularity of such taxation whatever. A striking example of the Government's lack of control over the provincial administrations is afforded in the case of a so-called dyke (or conservancy) tax on oil and benzine in the Province of Hunan. The proceeds of the tax have for some time past formed a useful part of the provincial revenues, and are apparently used for local reconstruction purposes (though not for dyke-building) with reasonable honesty. The tax formed, however, the subject of very strong protest by the foreign oil companies, who have their own taxation arrangements with the Central Government, and the Government first of all vainly ordered its abolition, with the intention of

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transferring the purposes of the tax to its own National Flood Relief Commission, and then ordered the Maritime Customs to take over its collection. This action was, however, likewise strongly resisted by the provincial administration, and the instructions to the Customs have had to be cancelled.

The budgets of the two last financial years have been balanced at 714.5 and 683 million dollars respectively, small amounts in comparison to the potential wealth of the country and those of other great nations. No less than 310 million dollars in loans were borrowed during 1930 and 1931 to meet the attempts made to overthrow the Government. Military expenditure for the last four fiscal years has amounted on the average to 45 per cent. of the total expenditure of the Central Government; in the last two fiscal years it has employed over 300 million dollars of the national revenue, though now it has been reduced to a figure of 18 millions a month, or 216 million dollars a year, the amount decided upon at the National Financial Conference of November 1931, representing another economy of roughly 100 million dollars a year. This does not, of course, represent the whole military expenditure of the country, or the whole burden on the people, for the semi-independent militarists, as shown above, raise local taxes in order to support their own armies. A new law governing the supervision of local finances was recently adopted by the Legislative Yuan at Nanking. This law forbids any provincial or municipal government imposing any new taxes, increasing existing taxes, or issuing any public loan without the sanction of the Ministry of Finance. Similar legislation has made its appearance before, but it is hoped no doubt that the new law will strengthen the hands of the Government in its struggle for control over local revenues.

187. The large increase in the customs revenue as a result of the new tariffs of 1931 is not expected to be maintained for 1932. The revenue for 1931 was 385 million dollars, the highest recorded, while that for 1932 is estimated to be only 285 million dollars, or a drop of 100 million dollars. The loss of the Manchurian customs revenues, on the basis of the 1931 figures, will account for roughly 40 million dollars of this decrease. The salt revenues amounted to 163 million dollars for 1931, and are estimated at 149 million dollars for 1932. The budgets for the last two fiscal years, however, show large sums of approximately 50 million dollars every year as "Transfers to local authorities from the Salt Revenue Inspectorate," in other words, revenues retained by the local authorities and not remitted to the Central Government at all. The Minister of Finance claims, however, that the foreign loan quotas are now being received with commendable regularity from all the provinces except Manchuria. In September communications were addressed by the Waichiaopu to the British, French and American Legations in regard to seizures by the Japanese and Manchukuo authorities of the customs and salt revenues in Manchuria. It was pointed out in these communications that such seizures seriously endangered the payment of the obligations secured on the customs and salt revenues, and that, as regards the former, the revenues for June and July fell short of the obligations payable therefrom by 3 million Shanghai taels. It was thought that these announcements might be the prelude to defaults in payment of the instalments of the customs and salt-secured loans falling due in September. Any such intention was, however, denied by the Minister of Finance, and no defaults actually took place.

188. The balancing of the budget unfortunately does not mean that China has met all her obligations, nor does the Minister of Finance hold out any hope of a speedy solution of the problem of the debt in arrears, discussion of which was begun at the informal conference held in Nanking in November 1930, and has never since been resumed. Dr. Soong goes so far as to say that, at a time like the present, when Government finance is barely holding its own, the bondholders cannot expect a comprehensive plan of settlement to be evolved; he contents himself with the vague assurance that, as soon as the financial and economic situation permits, negotiations will be resumed.

189. The railway loans alone, in which British investors are interested, were in arrears to the extent of over £5,500,000 of amortisation in the middle of the year, and interest payments to the extent of £4 million. The Ministry of Railways itself assessed the liabilities of the various State railways at the high figure of 1,353 million dollars to the end of June, including 320 millions for the Manchurian railways. It has been said that the net income of all the State

railways, as at present operated, would not suffice to pay the interest alone on this debt.

190. In spite of the spectacular manner in which the Minister of Finance has weathered the storms of the past year and put a stop to accumulation of internal debt, it is still abundantly clear, as he himself warns his countrymen, that future stability is dependent on the absence of civil war and freedom from external aggression.

191. The following are items in the story of Chinese finance for the past year which are perhaps worthy of separate mention:—

Shanghai Rehabilitation Loan.

192. A loan for 6 million dollars under the above title was floated in November by the Municipality of Greater Shanghai for reconstruction of the areas devastated by the Sino-Japanese struggles early in the year. It was underwritten by a British firm, Messrs. Benjamin and Potts, and the service is to be undertaken by the Hong Kong and Shanghai Bank. The loan, which is to be redeemed in twenty years, was issued at 85, at 6 per cent. interest, and is secured on the revenues accruing from the Shanghai municipal wharfage dues, with a supplementary lien on the customs revenues. It is said that these are the first internal loan bonds ever to have been underwritten by a foreign syndicate. The assistance given by the British interests concerned received much laudatory press comment.

China Merchants' Steam Navigation Company's Loans.

193. The conversion of this company into a State enterprise, mentioned elsewhere in this report, was the outcome of the abortive efforts of the previous general manager, Mr. Li Kuo-chieh (known as Marquis Li), who had only occupied that post since March last, to transfer most of this, the leading Chinese, shipping company's valuable properties to an American firm (the China Realty Company) in return for loans, which, if the whole scheme had materialised, would have amounted to some 30 million taels. In a connected agreement the Dollar Steamship Company undertook to purchase for the company thirty steamers for the coast and river trade; the ships were to be under the American flag as the property of the Dollar Company until paid for, and to be exempt from any laws that might be enacted regarding foreign-owned vessels operating in the coast and river trade of China. Mr. Li was subsequently placed under detention, and has now received a sentence of three years' imprisonment in the Chinese courts. The agreements, which were subsequently repudiated by the Government, were signed in September, and, besides the signature of Marquis Li, were sealed with the official seal of the then Vice-Minister of Communications, Mr. Chen Fu-mo, who is accused of receiving a bribe of 400,000 taels, and who has now absconded to Hong Kong. The Government is taking over the shares of the company at an arbitrary price of 50 taels a share, and Mr. O. S. Lieu, a well-known local business man, has been appointed general manager, with a board of directors and a board of supervisors composed of local bankers and other notables. In connexion with these developments, His Majesty's Chargé d'Affaires has reminded the Chinese Government of the mortgage rights of the Hong Kong and Shanghai Bank over the company's properties. The amount due to the bank under this mortgage executed in December 1923 is some 7½ million taels.

Japanese 30-million Gold Yen Loan for Manchukuo.

194. It was reported in November that a loan for this amount was being issued in Japan for the restoration of peace and order, the building of roads and the repairing of flood damage in Manchukuo. The loan was secured on the salt revenues of Kirin and Heilungkiang Provinces, and on the opium monopoly revenues; it was issued at 96.50 yen per 100-yen bond, interest at 5 per cent, redeemable in seven years. The Japanese banks appear to have been lukewarm about the issue, and to have invited the participation of the English, American and French group banks interested in the consortium for loans to China. The Manchukuo representative in Japan notified His Majesty's Ambassador at Tokyo that the Governments of Great Britain, France, Italy and United States of America had been informed of the loan project, and that subscriptions would be welcomed from European and American capitalists. It is not known-that any such assistance was forthcoming.

V.—TRADE.

195. As it has been necessary to prepare this report before the end of the year, and customs figures, &c., for the whole year are not available, the following notes cover only the first nine months of the year.

196. Considering the local difficulties and problems which have beset China in recent months, the foreign trade of the country for the first three-quarters of 932 has been well maintained. True, the average value of monthly imports January-September 1932 at 93 million haikwan taels shows a 23 per cent. decline from the monthly average of 120 million haikwan taels for the whole of 1931, while exports at an average monthly rate so far this year of 44 million haikwan taels record a decline of over 40 per cent., compared with the monthly average of 74 million haikwan taels for 1931. These are serious decreases, but less in degree than those of some other countries enjoying more stable government and complete freedom from banditry and its attendant evils. Unfortunately, however, one cannot be optimistic as to the immediate outlook, for political difficulties, the continued serious and costly bandit menace, some of which is coloured with a communistic tinge, the increased customs duties, and the consular invoice scheme, which, in its present form, would appear to be more for revenue than for facility to traders, and the detachment of Manchuria, are a combination of adverse conditions which it will take some little time to overcome.

197. But while her foreign trade declines, China is, to a greater extent than is generally realised, increasingly providing for many of her own needs by producing finished goods which formerly were imported. This is particularly true of textiles, although by no means confined to that trade. Imports of textile machinery in 1931 were valued at over 14 million haikwan taels, and in the first nine months of 1932 at just under 7 million haikwan taels. The total value of all machinery imported in 1931 (excluding railway equipment, motor cars and electrical materials and appliances) was 52 million haikwan taels, and in the first nine months of 1932 over 26,600,000 haikwan taels.

198. Practically all such machinery was for the equipping of Chinese industries, and the resulting increased production locally of finished goods accounts in some measure for decreased imports. Chinese imports of consumable manufactured goods are to a large extent for the foreign population and for the limited number of well-to-do Chinese. This trade will continue to be supplied by imported goods, but not necessarily to an increasing extent, at least until a higher standard of living is more widespread. Increased industrialisation is beginning to be considered by many of the influential and governing classes in China as the prime means through which China will be able gradually to get out of her difficulties and march on the road of modern progress towards equality with other nations.

199. The published records of the import trade of China for the first nine months of 1932 present some unusual features in the shares secured by the principal countries of supply.

200. The following table quotes the position covered by the period January–September 1932, compared with 1931 (full year):—

Imports

	to be a	Percentage of Total from—						
mo di sta di q	Total Value.	United Kingdom.	Germany.	Japan.	United States.	Hong Kong.		
1931— Jan.–Dec. (12 months)	Haikwan taels. 1,443,386,000	8.6	6.0	20.4	22.4	13.3		
1932— Jan. (1 month)	103,624,000 166,247,000 263,134,000 394,299,000 516,149,000 616,436,000 837,241,000	8·9 9·1 9·9 10·3 10·4 10·6 11·3	6·6 6·0 5·9 6·0 5·9 6·1 6·7	8·7 10·8 11·9 13·1 13·8 14·6 14·2	37·2 34·8 51·3 27·5 27·1 26·5 25·8	4·8 5·8 6·2 6·7 6·3 6·1 5·7		

201. Since January of this year the United Kingdom share shows a steady increase from 8.9 per cent. to 11.3 per cent. due mainly, but not entirely, to the anti-Japanese boycott. Many United Kingdom products are now more attractive to purchasers on account of their increasingly competitive value—a value not alone due to the abandonment of the gold standard by the United Kingdom. Japan's position has improved rapidly since the beginning of the year, but there are still signs of the boycott in several lines of Japanese merchandise, which may quite likely check that trade. The reduced share of the import trade credited Hong Kong is explained by the fact that since January of this year the Chinese Maritime Customs, in their records wherever ascertainable, have credited goods received from or via Hong Kong to the country of origin, instead of, as formerly, to Hong Kong.

202. The sharp decrease since January last in the share secured by the United States of America is due mainly to a decline in imports of wheat, raw cotton, kerosene and leaf tobacco from that country. All imports in January 1932 from the United States of America totalled 38,556,000 haikwan taels, of which 87 per cent. was for raw cotton, wheat, flour, leaf tobacco and oils. The comparative figures for June 1932 were 23,141,417 haikwan taels and 74 per cent., and for September 1932 were 16,882,602 haikwan taels and 70 per cent. It is estimated that total imports of manufactured products from Great Britain for the past twenty-one months have considerably exceeded the value of

the total for similar goods from the United States of America.

203. Based on the value of imports for the first nine months of this year, the total imports for the year 1932 will be lower than in 1931 by over 340 million haikwan taels. On the same basis exports for the whole year will be lower than in 1931 by no less than 360 million haikwan taels, and the adverse balance on account of visible trade will, on this estimate, amount to 580 million haikwan taels for 1932, compared with 525 million haikwan taels for 1931. It should be understood that the 1932 statistics for the Manchurian provinces are incomplete and only cover the half-year January to June inclusive. As, therefore, the figures for Manchuria are not available for July, August, and September, the above picture cannot altogether be accurate.

204. In view of the sharp decline this year in invisible exports, such as remittances from Chinese nationals abroad, funds for missionary work, &c., it is obvious that the import trade must still further decline unless some method of stimulating visible exports can be found. The shrinkage of the import and export trade has also seriously affected the Government income from customs duties, and the latter have been still further reduced by the withholding of the Manchurian customs collections.

Government Finances (see also under Finance, paragraphs 181 et seq.).

205. The financial position of the Government is very difficult. The net customs revenue for 1932 will not exceed 180 million haikwan taels,* compared with 243 million haikwan taels in 1931—a decrease of 63 million haikwan taels. The decline in revenue is due partly to the defection of Manchuria and partly to trade depression.

206. The recent increase of customs duties (see also paragraphs 217 and 218) on silk, wines, spirits, dyes, medicines, &c., is an attempt to increase Government revenue, but it seems more than probable that it will defeat its object. The importation of luxuries—silk, wines and spirits—will almost certainly decrease, while the increased duties on raw materials for industries—artificial silk, yarns, dyes, &c.—will hamper growing native industries.

207. The truth is that the Government of China has almost come to the end of its financial tether. The one remaining bulwark of its financial structure is the maintenance of the integrity of the customs in China proper. If that collapses, the bankruptcy of the Government cannot be averted. Every credit is due to the foreign staff of the Customs Administration for the way in which they have recently stood up to their increasing difficulties. Other services in China could be equally well and profitably administered if they were subject to a similar efficient direction. To take one example: The railways of China would, under efficient management, after rehabilitation, be remarkably profitable and

^{*} The actual revenue for 1932 amounted to 200,299,000 haikwan taels.

yield a very substantial income to the Government after all charges had been met. Not only so, but reliable transportation would develop the country, assist industry, and bring the products of the interior into the world's markets.

While it is true that the main source of the Government's income required to meet the service of the foreign and internal loans and indemnities is cured on the customs revenue, and therefore dependent on an adequate volume of foreign trade, it is equally true that 95 per cent. or more of China's huge population have no direct interest or concern in the matter. China, probably to a greater extent than any other country, is self-sufficing. The foreign trade of the country is the concern in the main of a handful of foreigners and a few leading Chinese merchants in the treaty ports. True, a fair volume of imports finds its way up-country through Chinese dealers. Likewise, produce from the interior comes down to the coast for export. But the total foreign trade of China is still a small thing both in its ratio to Chinese area and population and to the world trade. China's share of the total trade of the world is approximately 2 per cent.—her share of the world's population is between 20 per cent. and 25 per cent. The foreign trade of China is as yet unimportant to all but a few Chinese, though valuable to a number of foreign countries. If China is to take that increasingly important place in world trade to which the industry of her millions of hard-working and clever people and her natural resources entitle her it is clear that some form of guidance and co-operation from other friendly nations is required.

209. China to-day has reached a point in her life from where modern commercial development can be undertaken on a major scale provided reasonably peaceful conditions prevail. The last twenty years or more of struggle has demonstrated a capacity by the Chinese people for industrialisation, for adaptability to modern methods, and for production at prices which would ensure Chinese goods a substantial share in the trade of the world.

210. The lesson for the United Kingdom is, or should be, the obvious one of the opportunity that is presented for equipping China and her industries. Such an enterprise cannot be entered into without consultation and close co-operation with Chinese interests and careful examination of the merits of each proposal. The United Kingdom is excellently equipped to supply what is needed in expert guidance, experience, machinery and finance.

VI.—CUSTOMS AND TARIFFS.

211. For yet another year the Customs Administration, under Sir Frederick Maze, has weathered the storms that constantly beset it, whether in the form of encroachments on its functions by other departments of the Chinese Government, or of curtailment of foreign control in the higher branches of the service. As is pointed out elsewhere, the fact that the whole of the internal loan issue has since February last become a general charge on the customs revenues has strengthened the personal position of the Inspector-General as a trustee for the bondholders, though the policy which tends to identify the post of Inspector-General still more closely with the custodianship of the domestic loans was strongly criticised in the case of his predecessors.

Custodianship of Customs Revenues.

212. Changes necessitated by events have taken place in the methods of payment of the customs revenues from the various ports to the Inspector-General in Shanghai, which practically render the so-called custodianship arrangements of 1912, arising out of the peculiar circumstances of the revolution of 1911, a dead letter. Nowadays, the customs revenues are remitted from all over China to the Central Bank of China, the organ of the National Government, for the Inspector-General's account, and he draws thereon to pay the Hong Kong and Shanghai Bank, the sole remaining foreign "custodian" bank, the loan and indemnity quotas, and to meet the other charges on customs revenues, such as the domestic loans. Since all the customs revenues are now, in the first instance, paid into the Central Bank, the value of the security offered by the eventual payment of the loan quotas to the Hong Kong and Shanghai Bank is not so great as it

was when the revenues were remitted direct to the foreign banks. The systematic transfer, however, of gold units—the currency in which the import duties are now assessed and in which the greater part of the revenues are paid—to the Hong Kong and Shanghai Bank is a valuable power in the hands of the Inspector-General, which, in case of emergency, he could no doubt make use of by more frequent transfers, as he has entire discretion as to the level at which he keeps his accounts with the bank.

Smuggling.

- 213. As the Minister of Finance remarks in his recent statement to the 3rd Plenary Session of the Central Executive Committee of the Kuomintang, there has been a marked increase in smuggling, due no doubt to the increases in the tariff, along the coasts of China, particularly in the Canton delta from Hong Kong, and more recently on the Hopei (Chihli) and Shantung coasts from the new State of Manchukuo. The customs is building a number of patrol boats to cope with the situation. These activities have been responsible for a great increase in the severity of the fines levied by the customs on foreign shipping companies, where contraband or smuggled goods have been found on their vessels. These penalties have caused great dissatisfaction among the companies concerned, who contend that in cases where neither they nor their officers have been guilty of any negligence, it is unjust to inflict heavy fines for the discovery of goods smuggled by passengers or members of their native crews, and that the "annual guarantees" furnished by the companies to the customs in respect of their vessels call only for a reasonable degree of precaution on the part of the masters. The customs have, however, the whip hand of the companies in that, if the fines are not paid, they threaten to withdraw the extra-treaty "privileges" accorded to foreign vessels, such as the right to work cargo out of office hours, &c. The question has recently been taken up semi-officially with the Inspector-General of Customs on the companies' behalf.
- 214. Two questions of major importance connected with the customs have occupied the attention of this Legation during the past year. The first is the institution of a system of consular invoices to accompany all goods imported into China from abroad, and the second the seizure of the Manchurian customs-houses, resulting in the establishment of a separate customs administration for the new State of Manchukuo (see under Manchuria).

Consular Invoices.

215. Regulations governing the issuance of consular invoices were promulgated by the National Government on the 11th June and communicated by the Waichiaopu to the Legations shortly afterwards. They provided that, from the 1st September, all merchandise imported into China from abroad, with the exception of articles exempted from customs duty, must be accompanied at the time of embarkation with consular invoices sealed at the nearest Chinese consulate; this process was liable to involve examinations by the consul of the sales contracts, invoices or other relevant documents. The fee for certification was to be 2 customs gold units (8s. 3d.), and merchandise not so covered was to be liable to a fine equal to three times this fee. The minimum value of consignments for which a consular invoice was required was 200 Mexican dollars. The regulations were introduced with great suddenness and without consultation with the Maritime Customs, whose business it was to enforce them, and immediate objections were raised by the commercial communities, chiefly on the ground that the organisation of the Chinese consular service abroad was not extensive enough to make such a system workable (for instance, there was only one Chinese consular office in the United Kingdom and only three in the United States of America). The Chinese sought to meet this objection in the Detailed Enforcement Rules, promulgated by the Ministry for Foreign Affairs on the 25th June, which laid down inter alia that the functions of consular endorsement of invoices might be performed instead by commercial attachés, Chinese chambers of commerce or by consular officers of other nationalities. The objections to such compromises, on the score of the leakage of commercial information, were, however, equally apparent. His Majesty's Government asked for the postponement of enforcement of the regulations for six months, to permit of consideration of these and other minor difficulties, though no objection was raised in principle. The Chinese Government would not agree to postpone the regulations, but they were subsequently modified to the effect that consignments shipped from abroad during the months of September and October would pay 5 gold units only on arrival, those shipped in November and December 10 and subsequent consequent consignments the full penalty of 15 gold units; a private assurance was, however, given by the Waichiaopu that the period of two months without fines would be extended a further two months, so that no goods shipped from abroad before the end of the year would have to pay more than 5 gold units on arrival, even if unaccompanied by any invoices; this assurance was made public early in November.

216. Owing to the absence of any Chinese consular representative at Hong Kong and the objections consistently held by the Government of the Colony to any such appointment on political grounds, a difficulty arose as to how invoices could be certified at that port. After negotiation between His Majesty's Government and the Chinese Government, the appointment by the latter of a special officer, to be known as the "Chinese Invoice Officer," was agreed to and letters exchanged to this effect. The institution of this scheme for consular invoices was taken entirely on the initiative of the Ministry for Foreign Affairs, with the object of increasing the revenues of that Department; the Ministry were therefore strongly opposed to the suggestion, put forward by the Hong Kong Government, that the duties of certification of invoices should be entrusted to the Commissioner of Customs at Kowloon, an officer under the Ministry of Finance. It remains to be seen how the regulations will work in practice during the coming year, when the full penalty for non-compliance will be exacted.

Tariffs.

217. Increased import duty rates were introduced by the Chinese Government on the 4th August. The goods chiefly affected were mostly luxury goods, in the shape of silk articles, artificial silk, wines, medicines, toys, &c. The new duties aroused a certain amount of resentment in the foreign communities in China, as it was felt that they were designed purely for revenue-making rather than protective purposes, and that it was the foreigners in China who would have to foot the bill (see also under Trade).

218. It was decided to continue the collection of the full surtax of 10 per cent. on all import and export duties, imposed as from the 1st December, 1931, for payment of the American Wheat Loan (see paragraph 209 of last year's report), which was originally intended to be decreased to 5 per cent. after the 31st July, 1932, for another year from the 1st August, 1932.

VII.—THE BOXER INDEMNITY.

British.

219. Mr. G. E. McEwen has recently been appointed by the Chinese Government to fill the vacancy on the Purchasing Commission in London caused by the death of Mr. W. T. Charter. Sir W. Hornell having resigned from membership of the Board of Trustees in China in December 1931, the foreign members of the board are now Messrs. N. S. Brown, R. Calder-Marshall. K. Cantlie, W. H. Donald and A. J. Hughes.

220. Giving as their reason the sharp decline in customs revenues during the first few weeks of the year, the National Government proposed in February 1932 the temporary postponement for one year, beginning with the 1st February, 1932, and ending on the 31st January, 1933, of the payment of the British, American and Italian portions of the Boxer indemnity. It was pointed out that these instalments were not, like other indemnity funds, already pledged for loan service, and were being devoted to purposes beneficial to China, while the funds at the disposal of the various commissions administering them were sufficient to cover their requirements for one year. His Majesty's Government, in a note of the 18th April, 1932, agreed to the postponement as from the 1st March on the understanding that the purposes mutually beneficial to the two countries, to which the funds in question were devoted, would not ultimately suffer by the postponement, and that it would be for one year only and would not create a precedent; assurances to this effect were given in the Minister for Foreign Affairs' reply of the 29th April. The

United States Government returned a similar reply, though referring in some detail to cultural works (the China Foundation and Tsinghua University), which it was hoped would not suffer complete interruption. The Italian Government, whose position was different owing to the fact that the negotiations for the remission of their share of the indemnity had not been completed, agreed that the instalments accruing during the year in question, instead of being handed over to a Sino-Italian committee, which it was proposed eventually to set up, should used for the purchase by the Chinese Government of goods in Italy.

- 221. In paragraph 238 of last year's report it was pointed out that a question had arisen as to the relations of the Board of Trustees in China with the Purchasing Commission in London, in connexion with the placing of orders for material to be purchased in the United Kingdom with the latter body direct by various Chinese Government Departments, without the knowledge or approval of the board. This practice led to an open scandal in the early part of 1932, when the National Construction Commission, who were entitled, under the Chinese Government's system of allocation, to the use of a proportion of the funds, finding that certain electrical equipment which they required could not be purchased in the United Kingdom, changed their order to one for tin-plates and other similar materials. These they sold on the China market at some 20 per cent. below cost price in order to obtain funds, to the very serious detriment of the normal channels of trade in these commodities, as well as in opposition to the intention and spirit of the indemnity settlement. As soon as this action was brought to the notice of the Board of Trustees, steps were taken to remedy the situation, the board taking charge of the tin-plates, &c., not already sold, in order to sell them at their proper replacement value, the business being done throughout British business houses on a commission basis. Rules of procedure have now been laid down by which the Board of Trustees in China are placed in a position to control the purchase from indemnity funds of materials required by the several Chinese Government organisations, and all orders submitted to the Purchasing Commission in London have now first to be approved by the board.
- 222. Suitable arrangements have now also been made to secure the punctual payment of interest and repayment of capital, under agreements drawn up according to a specified form, by enterprises receiving loans out of the indemnity funds. A special committee has been established by the Ministry of Railways for this purpose. Criticism has been frequently directed at the Board of Trustees for their slowness in making grants to educational institutions, for which a large number of applications have been received, in pursuance of the terms of the indemnity settlement. The interest on the loans recently made by the board is, however, naturally accumulating slowly (it was stated to be only 100,000 dollars to the 30th June, 1932), so that it has not yet been possible to make any considerable grants for cultural purposes.
- Among the so-called "loans" for materials made by the board on account of the Ministry of Railways is that of £200,000 for the train ferry to cross the Yangtze between Nanking and Pukow, linking up the Shanghai-Nanking and Tientsin-Pukow Railways, which is expected to be in operation in the spring of 1933. Other grants of note on account of the same Ministry are those of £350,000 for equipment for the Kiaochow-Tsinan (Shantung) Railway, of £240,000 for the Tientsin-Pukow Railway and £110,000 for the Hunan-Hupeh section of the Canton-Hankow Railway, while a further advance of £200,000 was more recently made for the completion of the Han-Kiang (Hangchow-Kiangshan) Railway in Chekiang Province. Grants to other Departments include that of £140,000 for the purchase of electrical material to the National Construction Commission (see paragraph 221), £150,000 to the Ministry of Industry—subject to final approval—for the purchase of materials for the establishment of the National Machine Works, while a loan of £250,000 has been applied for by the same Ministry for the establishment of an ammonium sulphate factory in co-operation with German and British interests. The aggregate amount of the allocations actually made by the board at the 30th June, 1932, was over £1,500,000, of which some £1 million had been allotted to railways.
- 224. In the last few months of the year the Ministry of Railways have given their earnest consideration to various schemes for employment of most, if not all,

of the two-thirds of British indemnity instalments allotted to railways, partly for current expenses of, and partly as security for a loan for, the completion of the Canton—Hankow Railway, or for the purchase of materials to serve that railway. These schemes, and particularly the question of the security required by the Board of Trustees for such a loan, inevitably affect the prior rights of the group banks interested in the Hukuang Railways Loan Agreement of 1911, and of the bondholders who advanced the money for the construction of the string Hupeh—Hunan section of the line (this loan is over £2 millions in arrears), and at the close of the year no solution of the problem had been found. It will be remembered that this particular scheme, which has always found high favour with the Chinese Government for political and strategic, as well as economic, reasons, was strongly recommended by the Willingdon Commission of 1926 as a suitable object for the expenditure of the funds. British interests in Shanghai appear to be agreed that, if means can be found consonant with existing obligations, the use of the funds for a major project of this nature, instead of for divers small and scattered objects, would enhance British prestige in China. It is estimated that the completion of the line will cost at least £3\(^4\) millions, or about 60 million Mexican dollars.

Japanese.

225. Towards the end of July the Minister of Finance issued an order suspending payment of the monthly instalment (roughly £33,000) of the Japanese indemnity. This order elicited a storm of protest, and was subsequently withdrawn (it had been issued against the advice of the Inspector-General of Customs) on the ostensible ground that, in the meantime, a remittance of 843,675.44 Shanghai taels had been received from the Dairen branch of the Yokohama Specie Bank, representing about a third of the customs revenue detained before the seizure of the Manchurian Customs.

Dutch.

226. The Dutch Government are at present negotiating an arrangement with the Chinese Government for the remission of the Dutch share of the indemnity. Under this arrangement, 65 per cent. of the money is to be devoted to conservancy purposes, and 35 per cent. to cultural objects, such as endowment of the Sinological Institute attached to the University of Leyden. The Ministry for Foreign Affairs suggested that the former portion should be devoted to flood protection round Nanking, but Dutch interests want it to be used for surveys, &c., of new harbours to be undertaken by Dutch engineering concerns.

VIII.—AVIATION.

A viation Mission.

227. The Aviation Bureau at Nanking, under instructions from General Chiang Kai-shek, made enquiries in April as to whether His Majesty's Government would be prepared to send a Military Aviation Mission to China, the arrangement to include the training of Chinese aviators in England. Details of the probable cost of such a mission were conveyed to the Chinese Government, but nothing came of the proposal, and it seems probable that similar enquiries had been simultaneously addressed to the American and French Governments. A member of the Aviation Bureau stated that it had originally been the intention of the Chinese Government to establish an aviation school at Nanking for advanced training (which was to be British), while the American Aviation School at Hangchow (see below) was for the instruction of beginners; it was later, however, decided that the American school should undertake both functions.

Flying School at Hangchow.

228. There has been every indication during the year that definite efforts are being made to develop the Chinese air force, as being China's most profitable weapon of defence in the future. The Minister of Finance, Dr. T. V. Soong, holds this view strongly, and it is due to his initiative and influence that the School of Civil Aviation was established at Hangchow in July under Colonel John Jouett, formerly of the United States Army Air Corps. Colonel Jouett brought with him a personnel of some fifteen pilots, &c., formerly belonging to the United States army, including a medical officer for the testing of pilots. The cost of the school is believed to be in the neighbourhood of

200,000 dollars a month, provided by the Minister of Finance. Dr. T. V. Soong is said to have purchased, with his own funds on deposit in the United States of America, fifteen "Fleet" training machines now in use at the school. The present personnel under Colonel Jouett is to remain for three years. Their policy is to establish a high standard of training. The Chinese are believed to make very good pilots, if carefully selected; there are greater difficulties with Chinese mechanics, for they require more supervision than in other countries. It is said that advanced flying at the school will be carried out on Dougras machines. Twenty Italian Fiat B.R.3 1,000-horse-power bombing machines have also recently been sold to the Chinese Government under a contract signed by the Minister of Finance with the Italian Minister, the total cost being between 420,000 and 600,000 gold dollars. These machines will also be assembled at Hangchow, as they arrive. The first six, which reached Shanghai on the 3rd November, were accompanied by one Italian pilot and one mechanic.

Appointment of Air Attaché to China.

229. The projected development of aviation in China and the strong influence in aviation matters already gained by the Americans through the establishment of the aviation school at Hangchow, following upon the inauguration of the China National Aviation Corporation's air mail and passenger services (see paragraph 242 of last year's report), have caused His Majesty's Chargé d'Affaires to put forward proposals for the appointment of an air attaché to His Majesty's Legation. The proposal is strongly supported by the Commander-in-chief. Both the French and the Italian Legations already have air attachés, whilst American aviation experts are attached to the staff of the American Legation.

Hong Kong-Hanoi Air Service.

230. There has been considerable discussion during the year about the establishment of an air service between Hong Kong and Hanoi to link up either with the French service from Europe to Indo-China, or with the Imperial Airways services (at Rangoon or Karachi). Both a French company (Air-Orient) and a British company (the Far Eastern Aviation Company, of Hong Kong), are interested in this project, and have sought permission of the various authorities (French, British and Chinese) concerned to make the requisite experimental flights, which would necessarily be over Chinese territory. Five such experimental flights between the two places were carried out by the French company in the latter part of the year. The British company's application to establish an air mail service, flying over Chinese territory, has hitherto not been accorded. Permission to make an experimental flight was, however, given, but has not yet been taken advantage of.

Air Routes.

- 231. While no air routes have as yet been established with the co-operation of British interests, British aircraft hold their own in sales to the Chinese in competition with American, French, German and Italian planes, chiefly owing to the energy displayed by the two companies mentioned in paragraph 243 of last year's report, particularly in South China.
- 232. The Shanghai–Nanking–Hankow–Chungking service of the China National Aviation Corporation has been running more or less regularly throughout the year, and it is proposed, when political considerations permit, to extend the service from Chungking to Chengtu. The fleet of this company consists of seven Loening Amphibians and six Stinson-Detroiter land planes, though the latter are very rarely used. The total mileage flown by these planes in 1931 was 821,907 air miles, and the number of paying passengers carried 1,989, and of "pass" passengers 307. The Shanghai–Hankow section of this line is 850 kilom. long, while the Hankow–Chungking section is 870 kilom. The company has not yet availed itself of the exclusive right given to it in its agreement with the Chinese Government of July 1930 to run additional services between Nanking and Peking, and between Shanghai and Canton. This right was for three years, and therefore expires in July 1933. In the meantime, the Eurasia Corporation

have for a time operated a service between Shanghai, Nanking and Peking, which they propose shortly to resume.

- 233. The Sino-German Eurasia Aviation Corporation's service between Shanghai, Nanking and Peking, which it was intended to carry on across Manchuria to Manchouli, there to link up with the trans-Siberian Railway, has been suspended throughout the greater part of the year. This company has a feet of six planes—four Junkers W.33 and two W.50. One of the former type, and one of the latter type planes, crashed in accidents near Lanchow in Kansu in August 1932.
- 234. This company proposes to establish a service, avoiding Manchuria, between Shanghai and Tahcheng in Sinkiang, near the Russian frontier (4,050 kilom.), to link up with the Soviet services for carriage of mails and passengers to Europe. Soviet machines will carry the mails from the frontier to Moscow, and Lufthansa planes on to Berlin. This service will run through Nanking, Loyang, Sianfu, Lanchow, Suchow, Hami and Tihua (Urumchi). Conditions to Hami have been surveyed, but are uncertain beyond that point. Arrangements with the Soviet in regard to this service have not yet been completed.
- 235. Both these companies have received subventions from the Chinese Government, amounting to 3½ million dollars in 1931, all of which came from postal funds, a fact which was one of the main causes of the postal strike early in 1932. In spite of this assistance, the China National Aviation Corporation's services have only been carried on with the greatest difficulty, and the line is said to have only paid for itself during the Sino-Japanese clash early in the year, when communication between Shanghai and Nanking was maintained chiefly by air. The Chinese take readily to flying as passengers, though the price of tickets is too high to allow large numbers to travel. The fare from Nanking to Shanghai is 60 dollars by air, as against 17 dollars with sleeping berth by train. The manager of the company is reported to have said that co-operation between the company and British firms in running an air mail service between Shanghai and Canton would be suicidal to both interests.

Civil Aircraft.

236. There are very few real civil aircraft in China, except those used by a few military and political leaders for their own locomotion. Practically all civil aircraft imported are converted to military use, chiefly by fitting armaments locally. No register of aircraft is kept, and no proper pilots' certificates given (the latter may be remedied if the necessary powers are given to the Hangchow school). At Canton, there is no civil aviation proper. Various schemes have been drawn up for the purchase of aeroplanes by public subscription, but these have been dropped as entailing too great a burden on the people. Recently, Marshal Chen Chi-t'ang produced a three-year reconstruction plan, in which a scheme of civil aviation is included for the second year. The plan is said to be to create an air force of some 400 planes in the next three years to replace the forty odd now at Canton. A sum of 300,000 dollars spread over five years has been provided in the Hong Kong Government's estimates for aiding civil aviation schemes in the Colony, and the aerodrome at Kaitak is being developed.

A viation in Manchuria.

237. Aviation in Manchuria has hitherto served strategic and political, rather than commercial purposes, but it has lately developed beyond the purely military organisation of the old régime, and the new services carry both civilian passengers and mails. Civilian aviation is still in its infancy; the general attitude towards it is one of apathy, but the Japanese are enthusiastic within the limit of their means and are becoming air-minded. Prior to Japanese military intervention, there was no aviation in Manchuria, apart from the nucleus of a military air force created by the Mukden authorities. Subsequently, services on a number of air routes were created by the Japan Air Transport Company, apparently in accordance with the military and political situation of the moment. Such were the Dairen-Mukden, the Mukden-Antung, the Mukden-Tahushan-Chinchow, and the Tunhua-Ninguta routes. Of these, the Dairen-Mukden route is scheduled to be restarted in January 1933. With the removal of the capital

to Hsinking and the shift of the political-military focus to the north, the other routes are unlikely to be revived, unless events develop in the Liaohsi and Jehol areas. New services were, however, started on the 3rd November, 1932, for mails and passengers, between the following places: Harbin–Ninguta, Harbin–Fuchin, Harbin–Tsitsihar (via Hailun), Harbin–Tsitsihar (direct), Shingishu (Antung)–Mukden, Dairen–Shingishu (Antung), and Changchun–Huining (Kainei) via Tunhua. With the exception of the Dairen–Shingishu (Antung) section of the Dairen–Tokyo route, all these services are run by the new Manchukuo for transport Company, while the Japan Tourist Bureau acts as agents both for it and for the Japan Air Transport Company. The Manchukuo Air Transport Company is a joint Manchu-Japanese organisation, with a capital of 3½ million yen, of which ½ million is subscribed by the South Manchuria Railway Company. The contribution of the Manchukuo Government is thought to be made up of the franchise and the aerodrome and landing sites. The company are said to be purchasing from the Japan Air Transport Company nine Fokker Super-Universal six-seater machines. Initial flights on the principal routes were made on the 3rd November. These services link up the new capital with Tsitsihar and the north on the one hand, and with Japan on the other; they also link the capital with the three regions, where insurgency is still rampant, the Chientao area and the eastern borders, the Koshan district, and at Tsitsihar with the eastern ridge of the Hingan, beyond which the whole of Barga is at the moment of writing in revolt.

IX.—LEGISLATION.

- 238. During the course of the Second National Civil Affairs Conference, formally opened at Nanking on the 10th December, General Chiang Kai-shek is reported to have made a scathing criticism of the policy of the Chinese Government of issuing voluminous laws and ordinances in utter disregard of the practical conditions of the country. He pointed out that a total of about forty different kinds of district autonomy regulations, consisting of 957 articles, were now supposed to be in force, and that the detailed regulations which had been drawn up by the various provincial Governments on the basis of these fundamental regulations were almost countless. How could the people, he asked, be expected to become acquainted with such voluminous laws, regulations and detailed rules, of which even those responsible for the enforcement of district autonomy could hardly expect to gain a complete mastery?
- 239. This criticism, though in this instance directed against a particular class of legislation, might be equally applicable in varying degrees to recent Chinese legislation in general. Apart, moreover, from the question of volume and practicability, the drafting of most Chinese legislative measures since the establishment of the National Government admits of considerable improvement if cohesion and clarity are to be preserved in the future, the main faults being the frequent absence of repealing acts or clauses, as well as of definitions of the principal terms used in the measures in question, and the omission of the dates of other legislation mentioned therein.
- 240. It should be observed, however, that some hope of improvement in the above respects may be derived from the recent establishment by the Ministry of Justice of a Compilation and Research Department for the special study of foreign laws and from the enquiries received from that Ministry with regard to legislation and legal works in the United Kingdom which may indicate a desire on the part of the Chinese Government to seek inspiration and guidance from existing models abroad. It is, on the other hand, difficult to dissociate this sudden access of interest in the legal codes of other countries from the fact of the pending expiry early in 1933 of the Shanghai District Court Agreement, and, in view of the considerable adverse comment on Chinese judicial methods and administration which have been forthcoming in anticipation of that event, not to suspect that the underlying motive is not so much a conscientious urge for reform as a deliberate intention to prepare in anticipation the most comprehensive collection of legal and legislative measures possible for production at the psychological moment whereby to counter embarrassing criticism.

- 241. This theory receives some confirmatory support from the record of legislative measures dealing with matters of a judicial nature, but whatever may be the motives, there is little doubt that the production of Chinese legislation in general has followed some more systematic plan than has been the case in the past.
- neasures were enacted dealing with police, prison and judicial administration alone, while in the one month of November an entire series of orders were circulated by the Ministry of Justice to the judiciary enjoining higher standards of morality and general efficiency in the execution of their duties. With the enforcement of the Code of Civil Procedure, moreover, and its enforcement law, on the 20th May the series of ordinary civil and criminal codes promulgated by the National Government were theoretically brought to completion, while the promulgation of the Administrative Actions Law and the Administrative Court Organic Law on the 17th November similarly completed the legislative measures initiated in the Law of Petitions of Appeal of the 24th March, 1930, to provide the private citizen with facilities for obtaining judicial redress against illegal acts of Government Departments. Rules promulgated on the 13th July dealt with the functioning of the Supreme Court, while the composition and jurisdiction of the various law courts were formally defined in the Law Courts Organic Law of the 28th October, which incidentally, though still unenforced, is reported by the Chinese press as likely to undergo revision in the near future.
- 243. Railway legislation appears to have been aimed at strengthening the control of the Central Government over the various lines. The Railway Law of the 21st July gives the Ministry of Railways definite statutory powers over all railway lines, while the inauguration of National Railway Administrative Committees, whose working bye-laws were promulgated on the 19th August, enables the Government to assume the direction of these railways over the heads of their own administrations, though the latter have on occasions been still able to defy the orders of the Minister of Railways. Other regulations deal with the improvement of through-traffic and freight liability arrangements.
- 244. Amendments promulgated on the 27th September of the Labour Union Law of 1929 and of the law governing the settlement of disputes between capital and labour of 1930 are apparently devised to strengthen the hands of the Government authorities in dealing with strike activities of labour. These were supplemented on the 5th October by a set of four rules governing the organisation of labour unions composed of seamen and postal, railway and electrical workers. Other labour legislation includes the Workmen's Savings Provisional Instructions of the 1st April, which were foreshadowed in article 38 of the Factory Law of 1929.
- 245. Among the principal commercial enactments of the year are an amendment of the Trade-Mark Law Detailed Enforcement Rules of the 3rd September; certain amendments to the Mining Law of the 23rd January; various rules dealing with the institution of and procedure for the newly inaugurated system of consular invoices; the revision on the 29th October of the Bank-note Issue Tax Law of 1931, probably in deference to the complaints of Chinese banking circles; Rules for the Encouragement of Industries of the 21st November; the Inspection and Testing of Commercial Commodities Law of the 14th December; the Provisional Ordinance for the Encouragement of Industrial Arts of the 30th September and two subsequent rules subsidiary thereto. This ordinance is open to the interpretation of affording to Chinese citizens as opposed to foreigners special patent rights in respect of registration and exploitation of industrial inventions.
- 246. With regard to shipping questions, reference must be made to the Inland Waters Navigation Rules of the 27th September; the Ships' Officers' Test Regulations, and auxiliary regulations for the issue of certificates of competency promulgated on the 16th August, but so far not put into effect; and the Organic Ordinance for the Sea Fisheries Administration Bureau of the 5th July, the main purpose of which is stated to be to assist and protect the Chinese fishing industry against the competition of Japanese interests. A series of Acts defining the constitution of the China Merchants' Steam Navigation Company as a semi-official mercantile organisation were issued in March, and

subsequently revised in September. On the total conversion of the company into a State enterprise in November a further set of regulations were published to cover the new constitution.

- 247. The Organic Law of the National Government did not escape revision, being subjected to a minor modification on the 15th March, and again on the 26th December, when articles 30 and 48, which provide for the composition of the Legislative and Control Yuan, were amended in fulfilment of a resolution adopted at the third plenary session of the Central Executive Committee, held at Nanking in December. The Organic Law of the latter, as well as of the Executive Yuan, had already been revised earlier on in the year. The organisation of the Mongolian and Tibetan Affairs and the National Finance Commissions have also been constitutionally modified.
- 248. The general principles governing the provisional organisation of the newly instituted Military Affairs Commission were formulated on the 11th March, and subsequently revised in July. Military and naval legislation in general has featured unusually prominently in 1932, perhaps on account of the desire for reforms in this respect in view of the bandit campaigns and the menace of foreign aggression. The Legislative Yuan adopted in April draft principles for a Military Service Law. Although this measure has not yet been proceeded with, the subject of conscription was revived at the fifth meeting of the Second National Affairs Conference, which adopted a proposal for the introduction of a system of compulsory service of all able-bodied males between the ages of 20 and 40 in a Peace Preservation Corps, which is to combine the functions of militia and police. Military legislation actually brought into force includes the General Staff Organic Law, Military Cavalry School Ordinance, and Regulations regarding the Import of Aircraft and Materials. Naval legislation consists of some lengthy rules governing service on board ship, inspection and examination ordinances, and the Revised Naval Ceremonial Ordinance.
- 249. Other legislative measures of note enacted during the year are the General Amnesty Ordinance of the 24th June; the Estimate Budget Law, and the Final Budget Provisional Regulations of the 24th September and the 25th October respectively; the Game Law promulgated on the 28th December; and the Provisional Rules for the Control of Private Radio Broadcasting Stations of the 24th November. Mention should also be made of four local autonomy measures promulgated on the 10th August, but not yet properly effective, namely, the Organic Laws for Municipal and District Councils respectively, and the laws governing the election of their members.
- 250. Since the establishment of the separatist Manchukuo Government, there has begun to flow a fresh stream of legislation, which on the whole, in so far as general outline and wording are concerned, bears a close resemblance to the legislation issued in China. Among the most important are the Manchukuo Organic Law and measures dealing with the opium monopoly, customs and shipping dues, investigation of factories, courts of law, consolidated tax and inspection of shipping.

X.—PROPAGANDA.

- 251. Generally speaking, it may be said that, during 1932, the Chinese Government has for the first time paid serious attention to the problem of organised propaganda in foreign countries. The interest excited abroad by the Shanghai hostilities and the Manchurian dispute have evidently convinced the Chinese Government of the importance of adequately presenting their case in the newspapers of the world, and it is understood that, with this end in view, the semi-official and Government-subsidised Kuomin News Agency has reached an agreement with Reuter's for the dissemination abroad of the official viewpoint of the Nanking Government on the Sino-Japanese dispute. Similar arrangements have apparently been made with the United Press and with the Transocean News Service (with both of which organisations Kuomin has been closely allied for the last two years) for the presentation of the Chinese viewpoint in the press of the United States and of Germany respectively.
- 252. In the latter part of the year, an arrangement was concluded by His Majesty's Government with Reuter's, whereby the daily British wireless news

bulletins picked up by His Majesty's ships in Chinese waters should, where possible, be handed to Reuter's agents for distribution to the Chinese press. Another notable development during the year was the opening of agencies in China by the French Havas News Agency, which is understood to be subsidised by the French Government. Until recently there apparently existed an arrangement between Havas and Reuter's, whereby the former in return for a practical phopoly of the South American field, left Reuter's a clear field in the Far East. His agreement has now been terminated, and Havas has now established agencies in the principal towns of China.

- 253. The policy of the Chinese Government as regards internal propaganda underwent no great change during 1932; semi-official organs, such as the Min Kuo Jih Pao of Shanghai, or the Peking Leader, which, early in the year were suppressed or voluntarily suspended publication as a result of Japanese disapproval, reappeared again under another name later in the year; in almost every large city the newspapers continued to be subsidised (and often controlled) by the local party organisation; while the Kuomin and Central News Agencies, subsidised by the Ministry of Finance and Propaganda Department of the Central Kuomintang headquarters, helped to disseminate the official viewpoint of Nanking. In addition to the above, the Government subsidises for propaganda several less well-known news agencies, and a number of foreign style periodicals, such as the Economic Bulletin, the China Critic, and the China Weekly Review, the last of which is reported to receive a subsidy of 18,000 Mexican dollars per annum. Increasing attention is also being paid to the possibilities of using wireless for purposes of propaganda, and in the course of the year two large broadcasting stations have been opened; one, situated at Chenju, near Shanghai, is under the supervision of the Ministry of Communications, while the other, a powerful station recently constructed at Nanking, is controlled by the Propaganda Bureau of the Kuomintang headquarters.
- 254. The Chinese Government have allotted 400,000 Mexican dollars for the construction of a Chinese pavilion in the forthcoming Chicago Exhibition and for the expenses of collecting native products in China to be transported to the United States of America.
- 255. No information is available regarding the expenditure of the Manchukuo Government or of the Japanese authorities in Manchuria upon propaganda. There exists, however, a Bureau of Propaganda in the Department for Foreign Affairs at Hsinching (Changchun), which periodically issues bulletins giving the Government's viewpoint on questions affecting Manchukuo. Needless to say, the tone of the press in Manchuria since the beginning of the Japanese occupation has been violently pro-Japanese.
- 256. At the end of September, a somewhat awkward situation was created by the action of the postal authorities in Shanghai in suddenly notifying foreign newspapers and periodicals published locally that failure to comply with article 7 of the Law of Publications (see paragraph 262 of 1931 report) and with the Detailed Regulations for its enforcement would result in withdrawal of postal facilities. While no serious opposition could be raised to compliance with article 7, which merely provides for registration with the Ministry of the Interior (in accordance with the practice observed in most civilised countries), considerable apprehension was felt with regard to the detailed regulations, which provided for a strict control by the Kuomintang of all publications whose subject matter dealt in any way with the party, and rendered their proprietors, editors and publishers liable to the application of certain objectionable penal clauses in the Law of Publications.
- 257. During his visit to Nanking and Shanghai in October, His Majesty's Chargé d'Affaires took the matter up with the Minister for Foreign Affairs and with the Mayor of Shanghai. While conceding that there could be little objection in principle to the request that foreign newspapers should register with the Ministry of the Interior, Mr. Ingram explained the difficulties of ensuring compliance by the British press with the detailed regulations. He suggested that the whole matter be reconsidered, and urged that, in the meanwhile, no drastic action be taken against publications which failed to register. These representations would appear to have had the desired effect, since at the end of the year

Dr. Lo informed Mr. Ingram verbally that, for the time being at any rate, the Chinese Government would not require the foreign press in this country to comply with the Law of Publications.

XI.—CLAIMS.

- 258. In the annual report for 1931 (paragraphs 264–265) mention was mage of the preparation of lists of outstanding claims of British subjects for presentation to the Chinese Government. Owing to the unfavourable developments in the political and economic situation in China, however, the present moment is manifestly inopportune for reviving the general subject of claims, and the issue has therefore been left in abeyance.
- 259. Nevertheless, individual claims, in consideration of the special circumstances of the case, have been taken up separately with the Chinese Government, of which the following are of particular interest:—

(a) Compensation for the death of John Hay Thorburn at the hands of the Chinese military (see paragraph 269 of previous annual report).

£1,000 paid on the 24th February.

(b) Claim for 10,000 dollars compensation for gross ill-treatment of Mr. Gabb at the hands of Chinese troops at Changteh in 1929. After repeated representations, the sum of 5,000 dollars was finally extracted from the Chinese Government, accompanied by a very vague intimation that a further sum might be available at some future date.

(c) Claims amounting to 4,482,608.77 dollars, for damage to the property of the British Cigarette Company at Hsuchow, Honan, during military occupation in 1927. An unsatisfactory reply was returned to His Majesty's Legation's representations with regard to this case, as also, it might be here recorded, to those in connexion with the large claims for looting at Changsha in 1930, and for confiscation of the International Export Company's sheep near Kweihua in 1927, referred to in paragraph 266 of the previous annual report

in paragraph 266 of the previous annual report.

(d) Five claims for looting of the Bible Churchmen's Mission at Lungchow, Kwangsi, in 1930, were settled by mutual agreement locally on the basis of a cash payment of half the amounts claimed.

- 260. A claim against the Chinese authorities in Manchuria in respect of losses incurred by British interests during the Sino-Soviet hostilities of 1929 was presented locally in 1931. Certain other claims which appeared to lie against the Soviet Government were examined by His Majesty's Government, who at the beginning of this year authorised the presentation through His Majesty's Embassy at Moscow of claims on behalf of the Produce Export and Asiatic Petroleum Companies for losses incurred at Hailar by bombing and commandeering of stocks respectively, as well as of claims amounting to over 100,000 yen on behalf of Lloyd's Underwriters in respect of consignments of tea and sugar covered by their policies, which were removed by Soviet troops from Chinese Eastern Railway warehouses at Hailar and Manchouli during the same period. The reply from the Soviet Government was tantamount to a denial of liability.
- 261. Little progress has been made towards the liquidation of the Nanking incident claims, as the Chinese Government, in spite of repeated reminders, instead of the promised monthly instalments of 200,000 dollars, only remitted a total of 400,000 dollars for the whole year, *i.e.*, 200,000 dollars in June and 100,000 dollars in September and October.
- 262. As might be expected, the Sino-Japanese hostilities in Manchuria and Shanghai have produced a new crop of claims. Lists of claims for losses at Shanghai were filed by British subjects at His Majesty's consulate-general at that port; these have been carefully examined and, after elimination of a number of unpresentable items, collated into lists ready for presentation to the Chinese and Japanese Governments. The claims for losses incurred in Manchuria fall into two categories: (a) Losses due to the occupation of Mukden by the Japanese forces in September 1931 and the subsequent elimination of the existing administrative authorities of the Three Eastern Provinces, as a result of which

foreign firms found themselves unable to obtain payment for materials, &c., previously supplied; and (b) damage to property by bombing, &c., and losses through commandeering of stocks in the course of the various campaigns all over Manchuria. Owing to the peculiar circumstances of the Manchurian situation, no hard-and-fast line of procedure has been possible in respect of the latter, each case being examined according to its merits. The Manchukuo Government, however, expressed a readiness at an early date to consider the former category claims, which, including those of other nationals, represent a total of some 12 million dollars, and created a special liquidation commission for that purpose. They have now proposed to meet these claims on the basis of two-yearly instalments of 35 and 20 per cent. respectively in cash and the balance in the form of long-term interest-bearing bonds. A member of Messrs. Jardine, Matheson and Co. (Limited), the principal British claimants, is now on his way to Hsinking (Changchun) to conduct negotiations on behalf of all the British interests concerned.

263. Representations have also been made on various occasions during the course of the year on behalf of the following British creditors, as opposed to claimants, of the Chinese Government:—

(a) British creditors of Chinese railways for materials supplied, including Messrs. William Forbes and Co., the suppliers of the famous Blue Train to the Tientsin-Pukow Railway in 1921-22, to whom alone a total of nearly 10 million dollars is now outstanding. The Ministry of Railways has been supplied with the statements of these various creditors; liability has not been denied, though the figures quoted by the creditors have, in many instances, been challenged and considerably pared down, especially in respect of interest for delayed payments. Private negotiations have been simultaneously conducted with the Ministry of Railways on behalf of the British firms concerned by Mr. Calder Marshall, chairman of the British Chamber of Commerce at Shanghai and a member of the British Boxer Indemnity Board of Trustees. Some progress appears to have been made, and a skeleton form of agreement has recently been drawn up to cover the Tientsin-Pukow Railway debts, which, it is hoped, will be accepted as the basis for more detailed discussion.

(b) Amounts due in respect of salary, &c., to British ex-employees of the Tientsin-Pukow and Canton-Hankow Railways. Informal discussions have been in progress at Nanking between representatives of the Chinese Government, His Majesty's Legation and the creditors, as the result of which the Ministry of Railways' assessment of the sums due, though in some cases considerably below the amounts originally claimed, was accepted by the claimants, and the Ministry, on its side, undertook to commence payment thereof by instalments

as from December.

(c) Amounts due in respect of salary, &c., to British ex-employees of the China Merchants' Steam Navigation Company. Following diplomatic representations, a meeting was held in July between the accredited representatives of the company and of the Officers' and Engineers' Guilds, at which the former made an offer of a payment of 20 per cent. of each amount in final settlement, which offer was not accepted. On the subsequent reorganisation of this company as a State enterprise in November, these outstanding debts were formally brought to the notice of the new general manager, Mr. O. S. Lieu. by His Majesty's consul-general at Shanghai.

264. In conclusion, mention should be made of the belated payment through the Ministry for Foreign Affairs of the debt to the Government of North Borneo, incurred by Mr. Kwei Chih during his tenure of the post of Chinese consulgeneral in the years 1922–27, amounting, with interest to date, to 6,202 · 51 dollars Straits currency.

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POLITICAL DEPARTMENT.

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Minute Paper.

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Events in China prevented H.M. Minister from producing this report at the usual time.

Passages of interest from the Indian point of view are:

Page 11-12 Sin Kraing

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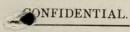
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CHINA.

Annual Report, 1931.

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Sir M. Lampson to Sir John Simon.—(Received June 22.)

(No. 507.) Sir,

Peking, May 3, 1932.

I HAVE the honour to transmit herewith the annual report on China for the year 1931. I am indebted for this work to the members of my staff, who have all, with their usual ability, contributed their respective sections and generally assisted in the preparation of the report.

2. I regret that it has not been found possible to furnish this report at the proper date. The crisis in Manchuria during the end of 1931, and the events at Shanghai at the beginning of 1932, have necessitated my absence and that of members of my staff from Peking for long periods, with the result that it has been found impossible to prepare all the sections of the report earlier in the year. I have, &c.

(For the Minister), ADRIAN HOLMAN.

Enclosure.

Annual Report on China for 1931.

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I.—INTERNAL POLITICAL SITUATION.

(1) General.

THE year 1931 opened with the prospects for the stabilisation of government in China brighter than they had been for some time past. As the result of the intervention of the Mukden faction on the side of Nanking in the previous autumn, the Northern rebellion led by Feng Yu-hsiang and Yen Hsi-shan had collapsed, and the whole country from Manchuria to Kuangtung was nominally united under the control of the National Government at Nanking. Looking below the surface, however, it was apparent that such stability as had been reached depended to no small extent on the continued collaboration between Chiang Kai-shek, who controlled the Government at Nanking, and Chang Hsueh-liang, who was established at Peking in military control of the situation in the North, and on the ability of these two leaders to maintain themselves in their respective positions. It was, moreover, no secret that the dictatorial methods of Chiang Kai-shek and the measures he had taken to restrain the activities of the Tangpu (local party offices) and their interference in governmental affairs were rousing more and more opposition against him within the ranks of the Kuomintang, and this not only amongst the section of the party, headed by Wang Ching-wei, which was openly and actively hostile, but also amongst some of the leaders of the governing régime, notably Hu Han-min, the President of the Legislative Yuan and the acknowledged political "boss" of that section of the Tang which was in power at Nanking.

2. The first two months of the year were, however, free from political complications, thus permitting the Government to take long overdue steps for dealing with the Communist bands in the interior of Kiangsi and Hupei and along the Yangtze between Hankow and Ichang. At the same time, preparations were set on foot for the summoning of the People's Convention in May in accordance with the resolutions of the fourth plenary session of the Kuomintang Congress, held at Nanking in the preceding November. Laws governing the election of the delegates for the convention were promulgated in January. It will be recalled that the object of this People's Convention, which was referred to in Dr. Sun Yat-sen's famous death-bed behest (the so-called "will"), was to settle questions concerning the tutelage of the nation during the revolutionary transition period before the constitutional era was reached. The political split in the ranks of the Nanking régime, which now ensued, concerned largely the question of what the functions of the convention were to be; and it soon transpired that the object of Chiang Kai-shek and his supporters was to utilise the convention to strengthen the position of the existing Government by giving it the appearance of constitutional legality and popular backing (as opposed to its being purely an instrument of the party) by the adoption of a "Provisional Constitution."

- 3. The friction between Chiang Kai-shek and Hu Han-min became more and more acute during the first two months of the year, and eventually culminated in the arrest of Hu Han-min on the night of the 28th February. According to the account of the affair given to His Majesty's Minister by the Minister for Foreign Affairs, Hu Han-min had resigned following a sharp difference of opinion with his colleagues of the Government on account of his uncompromising opposition to the proposal that the People's Convention should adopt a "Provisional Constitution." It was also given out that he was confined to his house by illness, suffering from high blood pressure. Actually Hu Han-min had been arrested and remained under detention for some nine months
- 4. Hu Han-min was too big a figure in the country and the Kuomintang to be suppressed without a stir, and the repercussion of these events in the provinces was anxiously awaited, especially in Kuangtung, Hu han-min being a native of Canton, the home of the revolution and the party. For some weeks nothing happened, and preparations for the summoning of the People's Convention continued apparently unaffected by General Chiang's coup in arresting Hu Han-min. As the month of April wore on, however, disquietening rumours began to be current of impending trouble at Canton. For some years now comparative peace and order had prevailed at Canton under the joint rule of two Cantonese generals, namely Ch'en Ming-shu, as chairman of the Provincial Government, and Ch'en Chi-t'ang, the local military commander. Ch'en Ming-shu, the commander of the Cantonese XIXth Route Army, was known to be a reliable supporter of Chiang Kai-shek, but the loyalty of Ch'en Chi-t'ang had long been in doubt.
- 5. The storm eventually burst on the eve of the opening of the People's Convention, when, on the 28th April, Ch'en Ming-shu and his adherents suddenly bolted to Hong Kong, leaving Ch'en Chi-t'ang, and other Cantonese leaders, in control of Canton. These latter proceeded to declare themselves by issuing a manifesto denouncing Chiang Kai-shek as a dictator and traitor to the people and the party. At the same time, most of the Cantonese members of the Nanking Government, including Sun Fo and Wang Ch'ung-hui, hurriedly left the capital for Shanghai. Soon after the news arrived that Sun Fo and Eugene Chen (who had reappeared in China a few weeks before) had gone to Canton; and it became apparent that the movement was a definite Cantonese secession from Nanking. A few weeks later a rival National Government was, nominally, established at Canton, including T'ang Shao-yi, Wang Ching-wei, Sun Fo, Eugene Chen, and Chen Chi-t'ang, and other local leaders. C. C. Wu, resigning his post as Chinese Minister at Washington, joined the Canton Government soon after. At the same time, peace was proclaimed between Kuangtung and Kuangsi, which had, after their usual custom, been intermittently at war for long past; and it was announced that the Kuangsi faction (Li Tsung-jen, Pai Ch'ung-hsi, and their Cantonese ally, Chang Fa-k'uei) had joined the Canton fold.
- 6. In spite of these alarming developments in the South, the People's Convention at Nanking was carried through according to plan, being in session from the 5th to the 17th May. Its principal task was to approve the proposed provisional Constitution, which was duly adopted. The provisions of the new Constitution of most immediate importance were those strengthening the position of the President of the Government, who, while being confirmed in the control of the national forces, was given the additional powers of appointing and dismissing the heads of the various yuan and Ministries.
- 7. The People's Convention was attended by Chang Hsueh-liang, whose presence in the capital served as a demonstration of the stability of the Mukden régime in the North, and the solidity of its support of Chiang Kai-shek and the Nanking Government. Actually the position at this time in the north was that Chang Hsueh-liang, backed by the resources of Manchuria, was established at Peking as Vice-Commander-in-chief of the National Forces, whence, while directly controlling the Peking-Tientsin area and the province of Hopei, he was in a position to exercise considerable influence over the rest of North China. Yen Hsi-shan had retired to Dairen. Feng Yu-hsiang was lying hidden in Southern Shansi. Honan was in the hands of Liu Chih, one of Chiang Kai-shek's most trusty generals. In Shantung, however, where Han Fu-ch'u remained in

control, the outlook was less reassuring, since General Han was known to be an old Kuominchun commander with affiliations in the camp of Feng Yu-hsiang. Moreover, Shih Yu-san, the notorious turncoat general, and a former associate of Han Fu-ch'u, was still in command of an army in Northern Central China, which was maintaining itself more or less "in the air" on the southern border of Hopei and Shantung.

- 8. Shih Yu-san had long been a disturbing factor in the situation in North China since his sudden coup at Pukow in December 1929, which had so nearly overthrown the National Government, and which had subsequently turned out to be the prelude to the northern rebellion which broke out in the following summer. After the collapse of the rebellion Shih had managed to save himself to some extent by tendering a nominal allegiance to Chang Hsueh-liang, but nevertheless found himself left out in the cold in the eventual distribution of the spoils of provinces and spheres of military control, made as the result of Chang Hsueh-liang's successful intervention. As the commander of a comparatively well-equipped army of 40,000 men, he could not be ignored nor, though recognised as a potential danger to the peace of the north, suppressed without serious fighting. From the moment when the Canton movement broke out into open secession from Nanking, trouble was inevitable with Shih Yu-san, for whom the opportunity was too good to lose. The north was full of inflammable material, such as the remnants of Yen Hsi-shan's Shansi troops and of Feng Yu-hsiang's Kuominchun, as well as Shih himself, and Han Fu-ch'u, a doubtful quantity, in Shantung. By July it was realised that trouble was definitely brewing and during the month the situation rapidly became increasingly critical. Towards the end of July it was known that Shih Yu-san's army had openly taken the field and was marching north with the object of advancing on Paotingfu, Peking and Tientsin. All then turned on the attitude of Shansi and Shantung, whose armies commanded the flanks of both Shih's advancing troops and the defending Manchurian forces. Shih's troops at first advanced northwards with little or no opposition, and occupied Shih Chia-chuang, the important railway junction of the Peking-Hankow and Shansi lines, from which the Mukden forces hurriedly withdrew. The latter claimed to have retired according to plan, and it was, indeed, obvious that, unless they could rely on the attitude of Shansi and Shantung, it was not possible for them to hold a line so far south and so exposed on either flank. Nevertheless, Shih Yu-san appeared to be meeting with spectacular success and it seemed that anything might happen. Government circles at Nanking remained confident, however, and insisted that Shih was walking into a trap. Whether planned or not, this turned out to be the case. Liu Shih, the Governor of Honan and a loyal supporter of Chiang Kai-shek, had set his troops in motion in Shih's rear, and in the last days of July reached and captured Shuntê, the chief town of Southern Hopei. The Mukden forces stood and fought at Tingchow in front of Paotingfu; Shansi forces descended on and occupied Shih Chia-chuang on the side of the Government; and Han Fu-ch'u in Shantung made no move. Shih Yu-san thus found himself hemmed in on all sides by hostile forces, his uprising having failed to call forth a single supporter amongst the doubtful elements by which he was surrounded. After a few days fighting the rebellion collapsed as suddenly as it had arisen. Shih's army rapidly dissolved, parts of it surrendering to the Government forces and others dispersing eastwards into Shantung, to be taken over by Han Fu-ch'u. According to press reports at the time, Shih himself made good his escape to Dairen. But it is typical of modern Chinese civil warfare (in which the defeated leaders seldom suffer any greater penalty than a temporary eclipse) that a few months later Shih Yu-san was living peacefully at Tsinan under the protection of Han Fu-ch'u.
- 9. Following on the People's Convention in May, the Central Executive Committee of the Kuomintang was in session at Nanking in June for the purpose, inter alia, of electing the personnel of the National Government, the composition of which was laid down in a new organic law promulgated in accordance with the terms of the Provisional Constitution adopted by the People's Convention. These events developed according to plan, confirming Chiang Kai-shek in his position as Generalissimo and President of the National Government, with Chang Hsueh-liang as Vice-Commander-in-chief of the National Forces. It was also decided to convene the Fourth National Party Congress of the Kuomintang at Nanking on the 10th October.

- 10. In the meantime the Cantonese movement remained curiously static throughout the summer, and little or no practical progress was made by the Cantonese leaders and their Kuangsi allies in consolidating a rival National Government at Canton. On the Nanking side Chiang Kai-shek and his Administration professed to treat the split as a purely political controversy to be resolved by pacific means, and to be determined to refrain from the use of military force. This, it was announced, was the decision reached at the session of the Central Executive Committee held at Nanking in the middle of June, when the necessity of concentrating all the available resources of the Government on the anti-Communist campaign in Kiangsi was determined upon.
 - 11. Chiang Kai-shek himself left Nanking on the 21st June to proceed to Kiangsi in order to take personal charge of the operations of the Government forces concentrated there for an organised drive against the Communist armies. It is believed that no less than 250,000 Government troops were employed for this purpose. The results of this anti-Communist campaign do not appear to have been decisive, and, while the Government forces were successful in so far as concerned the occupation of cities and districts, they seem, in actual fact, to have accomplished little but move the Communist bands on from place to place in the mountainous hinterland of Kiangsi and Fukien, where they continued to wage a guerilla warfare.
 - 12. Early in August Yen Hsi-shan, who had retired to Dairen after the collapse of the Northern rebellion in the previous autumn, returned secretly to Shansi. He made the journey of over 500 miles from Dairen to Tatung in a Japanese aeroplane, hired, so it was reported, for the purpose. It was significant that there had been strong rumours of Japanese intrigues in connexion with the Shih Yu-san rebellion and that Yen Hsi-shan returned to Shansi just at the moment when Shih's rebellion appeared to be meeting with success. The hostility of the Japanese to the Mukden Administration under Chang Hsueh-liang and their opposition to the latter tendering allegiance to the Nanking Government, were, of course, matters of common knowledge, and the friction between the Japanese and Chinese authorities in Manchuria was already giving rise to anxiety. To revert to the movements of Yen Hsi-shan, there was little doubt that he had returned to Shansi in the hope of being able to take advantage of Shih Yu-san's rebellion to recover his former territories and place himself at the head of his old army. The sudden collapse of Shih's rising prevented him taking any definite action for the moment, and he was reported to have retired to his home in the mountains of Shansi.
 - 13. It should be mentioned, in connexion with the situation in the North, that Chang Hsueh-liang, at the time of his visit to Nanking to attend the People's Convention, contracted typhoid fever, and that during the greater part of the summer he lay very seriously ill in the Peking Union Medical College Hospital at Peking, an unfortunate development, which may have had considerable influence on the subsequent course of events.
 - 14. In the early autumn the Cantonese movement took a more aggressive turn. Chiang Kai-shek and Nanking Government circles had throughout professed to minimise it and to be confident that the new Cantonese bloc, if left to itself, would break up of its own accord through internal dissension. There was, indeed, some justification for the contention that the rival National Government at Canton represented little but an ill-assorted collection of malcontents, comprising as it did among its principal constituent elements such irreconcilable personalities as Wang Ching-wei and Hu Han-min, who had been bitter opponents and rivals ever since the death of Sun Yat-sen, and, also, on the one hand, other left wing elements, including Eugene Chen, and, on the other, comparatively conservative Cantonese and Southern militarists, as well as the Kuangsi generals, Li Tsung-jen and Pai Ch'ung-hsi. Early in September, however, Wang Ching-wei and Chang Fa-k'uei, who had been in Hong Kong, returned to Canton, and reports were received that active preparations were on foot for a military expedition against Nanking. Three columns appear to have been set in motion, and before the middle of September the Southern forces had entered Hunan and had advanced without opposition as far as Leiyang, south of Hengchow. At this moment it was a matter of

speculation whether the Hunan generals and their troops would not join the Cantonese and thus enable the latter to repeat their successful invasion of Central China of five years before, when, in 1926, the Northern resistance had collapsed before the victorious advance of the revolutionary Southern forces. On the Nanking side reinforcements were hurried up to Changsha, and it was announced that Ho Ying-ch'in, the Nanking Minister of War, who had been directing the campaign against the Communists in Kiangsi, was proceeding to Hunan to take charge of the Government forces in their operations against the Southern armies.

- 15. At this moment, however, when serious hostilities were about to break out, the situation underwent a sudden change, and, about the 16th September, the news arrived that the Southern forces in Hunan, who had not yet established real contact with their opponents, were in full retreat on their way back to Kuangsi and Kuangtung. A day or two later came the Chinese-Japanese clash in Manchuria, and all talk of a Cantonese anti-North expedition came to an end. The decision not to proceed with the advance had, however, been taken, and the invading Cantonese troops were in full retreat from Hunan, before the outbreak of trouble in Manchuria. The real reasons for this sudden change remained a matter of speculation, whether the whole expedition was a bluff, or whether the underground peace negotiations, which had been proceeding intermittently for some time, had already produced results, or whether the Southern leaders had got wind of some counter-stroke being prepared by Chiang Kai-shek, whose armies had at last been meeting with some success in the campaign against the Communist bands in Kiangsi.
- Thus ended the Canton rebellion against Nanking, in so far as active military operations were concerned. In the meantime, the Japanese coup in Manchuria, dealt with elsewhere in this report, overshadowed the internal political situation. It was at first a question whether the Japanese stroke in Manchuria would have the effect of uniting the various contending Chinese factions in a common front against external aggression, or whether it might not encourage rebels and malcontents throughout the country, and thus promote further outbreaks of civil war. This was especially the case in the North, where the Japanese action had cut the ground from under the feet of Chang Hsuehliang, on whose continued co-operation with Chiang Kai-shek and the National Government at Nanking the peace of the Northern provinces was known to depend. Rumours were at first current that Yen Hsi-shan and Feng Yu-hsiang would seize the opportunity to square accounts with Nanking and Mukden and re-establish their authority in the North. But it soon became apparent that the national feelings roused by Japan's aggressive action in Manchuria were too deep and widespread to permit any Chinese leader taking advantage of the crisis for his own ends. And it was not long before Yen Hsi-shan and other leaders in the North issued manifestos pledging their support in resisting the Japanese invasion. At the same time, it was obvious that the position of the young marshal and his supporters, and their hold over the intra-mural regions of North China in their occupation had been rendered precarious, seeing that they had been deprived of their base in Manchuria. Their financial situation was also rendered acute in view of the fact that large bodies of Manchurian troops had been withdrawn within the Wall and required to be maintained on the revenues of the Peking and Tientsin areas.
- 17. In the South there were immediate and definite indications that events in Manchuria were to speed up the negotiations for a settlement between Nanking and Canton. On the 21st September, the Cantonese made the first move by issuing a circular telegram proposing that Chiang Kai-shek should voluntarily retire, that the Canton Government would then voluntarily dissolve itself, and that a conference should be called to organise a united National Government in the face of the danger from Japan. At the end of September Chen Ming-shu and two other delegates representing the Nanking Government proceeded to Hong Kong, where they met Wang Ching-wei and Sun Fo. Preliminary discussions at Canton followed. Before the middle of October Chen Ming-shu and the Nanking delegates left the South to return to Shanghai. On the 14th October Hu Han-min, who had been under detention at Nanking since the beginning of March, was released, and proceeded to Shanghai. General Li Chai-sum, who had been detained at Nanking since the spring of 1929, was likewise released, and

proceeded to Shanghai soon after. At the same time, both parties issued telegraphic manifestos emphasising the necessity for a united Government at this time of national crisis, and it was announced that a Unification Conference would at once be held at Shanghai. Finally, to facilitate a settlement, eneral Chen Ming-shu, the Cantonese leader, who, until the break with Nanking, had been at the head of the Canton local Government, and who had since remained loyal to Nanking, was appointed Garrison Commissioner for the Shanghai-Nanking area, in order that his XIXth Route Army (Cantonese) might be brought from Kiangsi to the capital and the neighbourhood of Shanghai, and thus reassure the Cantonese politicians as to their personal safety when they came

- Wang Ching-wei, Sun Fo, C. C. Wu and Eugene Chen, arrived in Shanghai. During the latter part of October and the first week in November, the Unification Conference was intermittently in session at Shanghai. Little direct information was available as to what passed at the conference, but, from such reports as appeared, it seemed that great difficulties were experienced in making any real progress. The Cantonese leaders pressed their demands that Chiang Kai-shek should relinquish his post and that the central military authority should be vested in a committee under the control of the civil Government; they also proposed that the Ministry of Finance should be subordinated to a financial committee, and that the Ministry for Foreign Affairs should be similarly subordinated to a special Foreign Affairs Committee such as already existed for dealing with the Manchurian crisis. Another stumbling-block in the way of the success of the conference was the insistence of Nanking on carrying out their plans for the holding of a fourth party congress in the capital in November, to which Chiang Kai-shek was, it was announced, prepared to submit all party differences, including his own position, but which the Canton delegates maintained would be but another packed and illegal assembly like the third congress held in the spring of 1929. There were also indications at this point of a split in the ranks of the Cantonese, namely, while Eugene Chen and Sun Fo maintained an irreconcilable attitude towards Chiang Kai-shek, Wang Ching-wei himself appeared to be showing some readiness to compromise with Nanking.
- 19. At length, however, a settlement of sorts was reached, and on the 8th November the conference dispersed after announcing that separate party congresses were to be held at Nanking and Canton, which would elect identical Central Executive and Supervisory Committees, which would in turn subsequently reorganise the National Government.
- 20. The Nanking Fourth Party Congress duly opened in the capital on the 12th November and sat until the 23rd November, and proceeded, amongst other business, to carry out the decisions of the Shanghai Unification Conference by electing members of the new Central Executive and Supervisory Committees as arranged. Resolutions were also passed restoring to full party membership the various political leaders expelled in the past, including Wang Ching-wei, the Kuangsi generals, and Feng Yu-hsiang and Yen Hsi-shan.
- 21. The stage was thus at last set for some sort of unification between Nanking and Canton, and it only remained for the Cantonese to hold their Congress and elect identical Central Executive and Supervisory Committees and then dissolve their Government. As usual, however, difficulties arose amongst the Cantonese politicians. Eventually, the Canton Congress opened on the 18th November, but in a stormy atmosphere. At first the decisions of the Shanghai Unification Conference were rejected, but eventually the politicians concerned were successful in patching things up and in inducing the local congress to pass the necessary resolutions and elect new Central Executive and Supervisory Committees in accordance with the decisions of the Shanghai Conference.
- 22. A new development now intervened at Nanking in connexion with the student agitation which, provoked by Japanese aggression, threatened, as in 1918–19, to submerge the Government. During the first part of December it became more and more apparent that the Nanking Government were at a loss how to handle the situation in face of the rising temper of the students, who,

as is traditional in China, defied the ruling authority to control or discipline their activities. On the 15th December the resignation of Chiang Kai-shek as President of the Government was suddenly announced. In accordance with statutory procedure, Lin Sen, chairman of the Legislative Yuan, assumed office as acting President. On the 16th December the Chinese press published General Chiang's circular telegram to the country announcing his resignation and the reasons for his retirement, namely, that it was absolutely essential in the national interests and in order to resist foreign aggression at this crisis in China's history that national unity should be achieved and an end put to internal strife; as the Cantonese were still refusing to proceed to the capital to attend the Plenary Session of the new Central Executive Committee until he, Chiang Kai-shek, had retired, he therefore tendered his resignation to the Central party authorities in order that national unity might be achieved and the country saved from destruction.

- 23. The way was now clear for the holding, at Nanking, of the plenary session of the new unified Central Executive Committee, including its Cantonese members, who had refused to come to the capital as long as General Chiang was President. On the 17th December Sun Fo, Eugene Chen, C. C. Wu and other Cantonese politicians, arrived in Nanking, where elaborate arrangements had been made for their reception. On the 22nd December Chiang Kai-shek left the capital by aeroplane for his home in Chekiang. With his departure the National Government, as it had existed under his presidency, practically came to an end.
- 24. On the same day, the 22nd December, the plenary session of the new unified Central Executive Committee, representing the Fourth National Congress of the Kuomintang, opened at Nanking. Friction soon developed with the Cantonese elements, but the first results of the discussions of the new committee were announced on the 24th December, when it was given out that agreement had been reached in regard to the proposed amendments of the Organic Law of the National Government. These amendments were designed to reduce the position of the President of the Government to that of a figure-head and to convert the chairman of the Executive Yuan into a sort of Premier at the head of a Cabinet composed of the chiefs of the various Ministries representing the machinery of Executive Government. The plans of the Cantonese in this connexion became more apparent when it was learned that Sun Fo himself was designated for the post of chairman of the Executive Yuan.
- 25. On the 28th December the proceedings of the session of the Central Executive Committee culminated in the election of the members of the new Government, which included Lin Sen as President, Sun Fo as chairman of the Executive Yuan, C. C. Wu as chairman of the Judicial Yuan, and Eugene Chen as Minister for Foreign Affairs. The other posts in the Government, including the chairmanships of the various Yuans and Ministries, were divided up amongst the various factions in the Kuomintang. The members of the Standing Committee of the Central Executive Committee and of the National Government Committee were also elected so as to include representatives of the various factions. The Standing Committee of the Central Political Council was confined to three names, namely, Chiang Kai-shek, Wang Ching-wei, and Hu Han-min, the three great rivals, who, ever since the death of their master Sun Yat-sen, had contended for the leadership of the Kuomintang. On paper the reunification of the party was complete, but in actual fact only nine out of the thirty-six members of the Government Council were in Nanking when the new régime was inaugurated on the 1st January, while all three of the party leaders above mentioned remained in retirement pending developments. And it was indeed common knowledge that, whatever prospects there might be of Wang Ching-wei making at least a show of working with Chiang Kai-shek, it was difficult, if not impossible, for Hu Han-min, embittered by old enmities and jealousies, to co-operate with either.
- 26. A noteworthy development at this point was the return to the political scene of Marshal Feng Yu-hsiang, who, since his defeat with Yen Hsi-shan in the civil war of the summer of 1930, had remained in retirement in Southern Shansi. After the Shanghai Unification Conference he emerged from his place of hiding and proceeded to Nanking where he joined in the deliberations of the party leaders.

27. There remains to record the changes brought about by these events in the occupancy of the post of Minister for Foreign Affairs. On the 28th September a mob of students stormed the Waichiaopu, forced their way into the office of the Minister for Foreign Affairs, and belaboured Dr. C. T. Wang with fists and furniture, inflicting serious head injuries. It was believed that the affair was, in part at any rate, instigated by motives of personal and political enmity, though the outward pretext was the indignation of the students with the policy of the Government vis-à-vis Japan. Dr. Wang, who had played so leading a part in Chinese affairs as head of the Waichiaopu during the past three years, immediately tendered his resignation, which was accepted on the 30th September. Mr. Alfred Sze, Chinese Minister in London, was thereupon nominated Minister for Foreign Affairs in his place, Mr. Frank Lee, the Vice-Minister, taking charge of the Waichiaopu as Acting Minister for Foreign Affairs in the meanwhile. Mr. Sze, however, was unable or unwilling to take up the appointment, and Mr. Lee remained in charge of the Waichiaopu for some two months. He was eventually succeeded by Dr. V. K. Wellington Koo, who had been a member of the special Foreign Affairs Committee entrusted with the conduct of the Chinese diplomatic case in the conflict with Japan and who had in this way come into prominence in connexion with the handling of the Manchurian dispute. Dr. Koo was appointed acting, and later officiating, Minister for Foreign Affairs and assumed office on the 30th November. His appointment, however, coincided with the student agitation, and he was scarcely able to function during his brief tenure of office, which came to an end when he resigned, with the other members of Chiang Kai-shek's Government, to permit the inauguration of the new Cantonese régime on the 1st January with Mr. Eugene Chen as Minister for Foreign Affairs.

(2) Manchuria and Dependencies.

(a) General.

- 28. Manchuria being economically the most highly developed part of China, was naturally the most susceptible to the effects of the world-wide trade depression of 1931; the foreign demand for Manchuria's principal export, the soya bean, was negligible, and merchants were in many cases unable to get rid of their stocks, even at prices which were a third of those ruling two years before. The decline in the value of silver had an equally disastrous effect upon the import trade, and the sales of foreign goods showed a marked decrease.
- 29. This stagnation of commerce had, as was inevitable, two important reactions upon the political aspect of the Manchurian situation. Firstly, unemployment led to a serious and progressive increase in banditry which was later in the year to afford Japan a good pretext for armed intervention; and, secondly, the hard times affected the Japanese trader much more severely than his Chinese rival, with his lower standard of life. The resultant decrease in the Japanese share of Manchurian trade caused alarm in Japanese business circles and led to vigorous propaganda in favour of "strong action" in order to prevent Japanese interests from being squeezed out of Manchuria.
- 30. In April Marshal Chang Hsueh-liang, leaving the administration of Manchuria in the charge of Chang Tso-hsiang, the Governor of Kirin, flew down to Nanking to attend the National People's Convention. On his way back from the south in June he fell seriously ill at Peking, and was admitted into the Peking Union Medical College, where he remained for some months. His headquarters were moved down to Peking from Mukden on the 18th July.
- 31. Meanwhile Sino-Japanese relations in Manchuria were, as is related in another section, deteriorating rapidly, and on the 18th September, when the young marshal was still convalescent, the Japanese overthrew his administrations in Liaoning and Kirin. A "Committee for Joint Regularisation" was provisionally set up at Mukden on the 25th September under the chairmanship of Yuan Chin-K'ai. The following day Chang Tso-hsiang was replaced by Hsi Sh'ia as Governor of Kirin. In Heilungchiang a Government loyal to the young marshal held out for some two months longer, and was finally extinguished with the capture of Tsitsihar by the Japanese on the 19th November.

32. At the close of the year the Japanese were in virtual control of all Manchuria save the Chinchow area in the south-west (which they were soon to occupy) and certain sparsely populated regions up near the Soviet border, where small bands of troops still faithful to the former régime maintained a precarious and ineffectual resistance. Already the Japanese higher command were toying with the idea of creating an independent Manchurian State and of placing at the head of it the ex-Emperor Pu Y'i, who had been smuggled out of Tientsin in November, and was being held at Port Arthur until he should be needed.

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(b) South Manchuria Railway.

- 33. The diminution of business suffered by the South Manchuria Railway during 1930 was intensified during 1931, as the world economic depression grew more acute. The difficulties of the railway were further complicated by the fall in the value of silver, which caused its freight charges, calculated on a gold yen basis, to rise in terms of local currency and thus allowed its Chinese competitors to undercut it by a comfortable margin. With a view to remedying the situation the railway administration early in 1931 inaugurated negotiations with representatives of the Chinese railways in Manchuria for the purpose of securing a revision of freight agreements in return for some concession as regards outstanding railway loans. The Chinese, however, who were naturally not anxious to alter a state of affairs so advantageous to them, succeeded by various pretexts in postponing the discussions, and no progress had been made by the Japanese up to the moment when the present Sino-Japanese dispute broke out.
- 34. In June Dr. Sengoku, on "grounds of ill-health," resigned from the chairmanship of the railway, and was replaced by the distinguished statesman Count Uchida. At the general meeting of the shareholders which took place a few weeks later it was revealed that the profits of the company for the year 1930–31 had dwindled to less than 50 per cent. of those for 1929–30, which was itself one of the most unsatisfactory years financially, experienced by the concern since the war. Japanese public opinion was unanimous in attributing this unsatisfactory state of affairs to the competition of Chinese "parallel lines," and a popular clamour arose in favour of strong action to prevent the South Manchuria Railway and Japanese interests in general from being squeezed out of Manchuria.
- 35. Since the seizure of Mukden by the Japanese in September last it has been difficult to obtain any information regarding affairs of the South Manchuria Railway. It is known, however, that advantage has been taken of the political situation to enlarge the railway settlements at Mukden and other points.

(c) Other Lines.

- 36. The fall in the value of silver was of no little benefit to the Chinese lines in Manchuria, and enabled them to compete successfully against their foreign rivals. The Chinese Eastern Railway, for instance, suffered heavily from their competition, and particularly from the opening of the new Tsitsihar-Koshan branch line, which tapped a rich area which had hitherto been the monopoly of the older line.
- 37. There is no doubt that the South Manchuria Railway during the first eight months of the year also felt the competition of the Chinese lines. Since September, however, it would appear that some arrangement has been evolved whereby the new Chinese lines, now under some measure of Japanese control, act as "feeders" to the South Manchuria Railway system.
- 38. Apart from the opening of the Tsitsihar-Koshan line and the inauguration of a somewhat irregular service along a section of the still uncompleted Taonan-Solun system, there was little progress in Manchurian railway construction during 1931. Survey work was undertaken in connexion with a number of projected lines, the most ambitious of which was the Kirin-Tungkiang system, which was to run roughly north-eastwards along the south bank of the Sungari River up to its confluence with the Amur. Japanese action in Manchuria has put an end to these projects, at any rate for the moment.
- 39. On the other hand, the Japanese appear to be taking advantage of their domination of the country to complete the extension of the Kirin-Tunhua line to

Kainei on the Korean border, where it will link up with a Japanese line running to the sea. The completion of this system will greatly facilitate Japanese access to Manchuria.

Mongolia.

- 40. Information regarding the situation prevailing in Mongolia continues to be meagre and unsatisfactory. All that can be said of it with any certainty is that in its broadest aspects it remained unchanged throughout 1931, while certain tendencies noted in previous years were accentuated.
- 41. In Outer Mongolia Soviet influence was increased by social reforms of a Communistic nature designed to strip the reactionary Princes and lamas of the last vestiges of power which remained to them. At the same time the Russians were able to tighten the economic stranglehold of the Soviet upon the country. A five-year plan of economic development, modelled upon the Plan of the Union of Soviet Socialist Republics, but adapted to the needs of a pastoral race, was brought into operation, and measures were taken scientifically to improve the strain of Mongolian horses and cattle. In order that Mongolian trade should continue to flow northwards into Siberia, the trade-route to Kalgan was kept firmly closed. In their efforts to kill the last vestiges of Chinese trade with Outer Mongolia the Russians were aided by the shortsighted policy of the Chinese authorities in Inner Mongolia, who mercilessly taxed all caravans which strove to pass through from the south.
- 42. Inner Mongolia remained uneasily quiet throughout the year under the feudal rule of a number of princelings who acknowledged the sovereignty of China. They regarded with suspicion the efforts of the Chinese and of the Kuomintang working from Kalgan to penetrate into their territories, but terrified by the example of Outer Mongolia, and by the intensive propaganda of Soviet agents within their borders, they chose allegiance to Nanking and a certain measure of Chinese supervision as the lesser of two evils
- 43. Since September the position in Inner Mongolia has been complicated by Japanese intrigues. It is impossible to determine the scope of Japan's ambitions in that region but it is known that she considers herself to possess "special interests" there under various secret Sino-Japanese agreements, and in recent negotiations regarding the Sino-Japanese dispute Japan has shown a tendency to treat the question of her "rights" in Inner Mongolia as being closely connected with the Manchurian issue.
- 44. Lately Japanese agents have been active among the Mongol princelings and are reported to have been offering them Japanese assistance in bringing about the unification on feudal lines of the two Mongolias, in return for Mongol armed support against the Chinese. It is impossible to say whether these proposals commend themselves to the Mongols. It is certain, however, that the Chinese are afraid that Inner Mongolia may at any moment declare her independence; and it was probably in an eleventh hour attempt to delay the seemingly inevitable that the Nanking Government in October last promulgated the Mongol League Tribe and Banner Organic Law; this appears to be an attempt to tighten Chinese control over Inner Mongolia by compromising with those feudalistic elements in the country which Republican China had in the past striven to destroy.

(e) Sinkiang.

- 45. Chin Shu-jen, chairman of the Provincial Government, continues to rule Sinkiang with an iron hand. His Administration is a despotic one, owing but nominal allegiance to Nanking. Neither the Kuomintang nor the Three Principles are regarded with much enthusiasm in Sinkiang, and the modern type of foreign-educated Chinese is even less welcome there than are Europeans.
- 46. The chairman's rule though severe is apparently efficient, and Sinkiang remains to-day one of the few regions of China where authority is respected and the roads are kept comparatively free of bandits. Nevertheless, there would appear to be a considerable amount of popular discontent in the province, particularly among the Turki communities. They complain that the extortions of the Chinese magistrates, who are now replaced annually and thus have but a short time in which to feather their nests, are more insupportable than ever before.

Nevertheless, this discontent, however general it may be, is not yet a serious feature politically, and the province remained quiet throughout 1931, save for an attack by Tungans upon Hami near the Kansu border, which was successfully repulsed, and a rising of Kalmucks in the Yuldiz valley of the Tien Shan. This latter revolt, which was settled by negotiation, is reported to have been due to Soviet instigation.

- 47. Soviet influence throughout the northern part of Sinkiang was steadily extended during the year, and in the summer an important commercial agreement was concluded between the Provincial Government and the Union of Soviet Socialist Republics. Details of this agreement are not yet known, but it is believed that under the terms of it Russia has secured the right to construct roads across the Irkeshtan border, to establish trade posts at a number of points, and that Russian traders may travel freely in the province.
- 48. Relations between His Majesty's consul-general at Kashgar and the Chinese authorities remained cordial throughout the year, although there were a number of minor disputes regarding jurisdiction over British Indian subjects. These were due to an increasing tendency on the part of the local magistrates to ignore British extra-territorial rights.
- 49. The balance of the arms and ammunition purchased by the Provincial Government from the Government of India were safely delivered in the autumn.

(f) Tibet.

- 50. Anglo-Tibetan relations were maintained during 1931 on the friendly basis established during Colonel Weir's visit to Lhassa in 1930. The arrangements made at that time with regard to the wool monopoly and to the supply by the Government of India of arms and of silver were put into operation, and worked satisfactorily, although the decline in the market value of wool disappointed the Tibetan Government of the profits which they had anticipated from the monopoly of this commodity. The only point which in the course of the year came up for discussion between the Tibetan Government and the Government of India was that of certain modifications of the Tibetan boundary in the Tehri region. This matter which was brought to Colonel Weir's notice during his stay at Lhassa may, in accordance with the request of the Tibetan Government, form the subject of negotiation between Tibet and India.
- 51. Sino-Tibetan relations exhibited during 1931 some curiously contradictory features. On the one hand the Dalai Lama appears to have maintained friendly intercourse with the Chinese Government, exchanging presents and telegrams with Chiang Kai-shek, sending delegates in the spring to the National People's Convention at Nanking, and even establishing a permanent diplomatic representative there. On the other hand, relations along the Tibet-Szechuan border were seriously embittered by the prolonged struggle between the lamasseries of Tache and Behru (see paragraph 59 of 1930 annual report). This dispute in the spring led to an invasion of Chinese territory by a powerful Tibetan force, who easily defeated the Chinese troops sent against it. The quarrel, punctuated by occasional truces, dragged on until the autumn, when a modus vivendi under the terms of which the Tibetans obtained a provisional adjustment of the frontier and other advantages, was concluded, thanks to the efforts of a representative sent up to Szechuan by the Committee for Mongolian and Tibetan affairs at Nanking.
- 52. Early in the year, the area along the Sino-Tibetan border previously known as the Szechuan Marches, together with certain districts in North Yunnan and South Ch'inghai, was formed into the new province of Hsikang, with its capital at Batang. A Kuomintang delegate was sent up by the Central Government to take charge of the new province, but owing to personal unpopularity, he is reported to have been unable up till now to take any part in local affairs.
- 53. The Tashi Lama visited Nanking during the holding of the National People's Convention. Honorific titles were showered upon him by the Chinese Government, and he was said to have been allotted a handsome subsidy, part of which was to be devoted to anti-British propaganda. On his way to his summer

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residence in Mongolia he visited Peking for a few days in July. He was reported at the end of the year to be living in Mongolia, somewhere to the west of Hailar.

54. No progress appears to have been made towards a reconciliation between the Tashi and the Dalai Lamas. The latter is, in fact, reported recently to have sued instructions that if the Tashi Lama should attempt to return to Tashilumpo, he should be arrested directly he set foot on Tibetan territory.

(3) Communism.

- 55. There is no evidence to show that during 1931 the Chinese Communist party has strengthened or improved its position or that communist doctrines have made any appreciable headway in China. On the contrary, at the beginning of the year it was fairly clear that the party was in danger of total collapse as an effective factor in Chinese social or political life owing to the lack of unity within its ranks. The absence of co-operation between the peasant and labour elements and the failure of the party to reach agreement upon any common line of policy were factors which were bound to lead to the disintegration of the machine, unless Moscow could reassert her influence over communist activities in the country. During the summer, the Red Armies in Kiangsi, although undoubtedly a standing menace, failed to make any considerable progress; their organisation was sadly deficient and their efforts to attract support from the ranks of their opponents met with but little response. Later, during the flood period the Chinese Communist party seems to have failed completely to take advantage of a particularly suitable moment for the development of its activities. On the other hand when the Sino-Japanese crisis in Manchuria occurred in September it seized the opportunity of spreading its doctrines, especially in Shanghai, under the guise of patriotic propaganda, with some measure of success. It is certain that the student demonstrations against Japanese aggression were to a large extent financed with Communist money and the result of Communist propaganda. In this connexion it is to be remembered that Communist literature is introduced into China and distributed efficiently without difficulty, particularly in Shanghai, industrial areas and some of the universities, and there is no reason to suppose that the supply of funds from Moscow has ceased. With regard to the supply of arms, it is admittedly true that this is insufficient and that the Red Armies rely mainly for their supplies on captures and desertions from the Government forces.
- 56. Following on the arrest in June at Singapore of a member of the Communist Organisation, the Pan-Pacific Trade Union Secretariat suspicions were aroused as to the activities of a certain Hilaire Noulens. His residence and office in Shanghai were searched and incriminating Communist literature discovered. He was arrested, together with a woman alleged to be his wife. They were eventually handed over to the Chinese military authorities and sent to Nanking for trial. At the end of October the Ministry for Foreign Affairs stated that the case had been referred to Chiang Kai-shek for his consideration and decision.

(4) Student Agitation.

- 57. Japanese aggression in Manchuria provoked an immediate and indignant reaction among the students, who hastily organised volunteer corps and propagandist bodies. At first they tended to support the Government in its policy of passive resistance, and there were indications that their activities were approved, if not encouraged, by the authorities. The movement, however, quickly got out of hand. The students began to clamour for war and for firearms to be issued to the newly-organised Volunteer Corps; and on the 28th September a crowd of angry youths from Shanghai raided the Waichiaopu and expressed disapproval of China's foreign policy by assaulting and injuring Dr. C. T. Wang.
- 58. Thereafter, for the next few weeks, the students remained fairly quiet, although in Canton on the 10th October police fired on and killed some student picketeers who had been destroying Japanese goods. About the middle of November, however, when it became clear that it required more than League action to eject the Japanese from Manchuria, the students began once more to clamour for war, for resumption of relations with Russia and for the recovery

of Manchuria by a punitive expedition to be led by Marshal Chiang Kai-shek in person. Encouraged by the Cantonese and the Communists, who saw in them a means of harassing the Nanking Government, the student agitations grew increasingly violent. At most of the educational institutions throughout the country, studies were suspended while student delegates proceeded to the capital to demonstrate in favour of war. Endeavours were made to put a stop to these pilgrimages by refusing free accommodation in the trains. The students' reply to this manœuvre was to lie down on the railway track, or to seize and occupy the railway stations until free transport was accorded them.

- 59. Despite the lenient behaviour of the authorities, the student movement as a whole had by now become intensely hostile to the Government and from the 4th December onwards there was throughout the country a serious epidemic of student rioting which only died down with Chiang Kai-shek's resignation. Of these disturbances the worst occurred at Shanghai between the 4th-8th December when the Tangpu offices were wrecked, the Shanghai-Nanking Railway line damaged, and the mayor imprisoned by an angry crowd for some twelve hours in the municipal buildings; at Peking about the same time when students lying prone upon the rails held up all railway communication with Tientsin; and at Nanking where on the 16th-17th December several thousand students raided the Waichiaopu, assaulted General Chen Ming-shu, attacked the party headquarters and smashed up the offices and plant of the "Chung Yang Jih Pao," a Government newspaper. At this point the Government reluctantly decided to take strong action, and most of the demonstrators were forcibly ejected from the capital. The situation was, moreover, still further eased a few days later by the resignation of Chiang Kai-shek.
- 60. One of the most significant features of these riots was the intense hostility manifested towards the Kuomintang. In Peking, Nanking, Shanghai, Hangchow and Taiyuanfu the students either wrecked or attempted to wreck the Tangpu offices, and at the end of the year signs were not lacking that their dislike for the party was no less violent than had been their former support of it.

(5) Floods.

- 61. Owing to the extremely heavy rains in July which fell in several districts of the Yangtze River Valley simultaneously Central and South China were visited with disastrous floods. The crops in the richest rice-producing regions of the country were completely destroyed, whole villages washed away and the inhabitants faced with famine and destruction. Hupeh Province, where several million people were rendered homeless, suffered the most severely and at Hankow the river rose to an unprecedented level. Here the food shortage became a serious problem and the excessive heat caused grave fears of the outbreak of epidemics. Nanking fared better, although large areas were inundated and the refugees reached a figure of 50,000. In the Wuhan area alone the homeless are reported to have numbered half a million. Many British firms suffered heavy losses, but no loss of British life occurred. The flooding of the Yellow River and the Huai River and the bursting of the embankment of the Grand Canal at the end of August, resulting in the inundation of large tracts of country, went to swell the number of homeless and destitute
- 62. Immediate steps were taken by the Chinese local authorities to cope with the situation and a National Flood Relief Commission was formed in Shanghai by the Chinese Government with an international committee to co-ordinate the activities of all existing relief bodies. On his arrival in China in October, Sir John Hope Simpson was appointed Deputy Chairman and Director-General of this commission. All possible assistance was rendered by His Majesty's ships at Hankow and elsewhere in the way of medical supplies, and at the request of the Minister of Finance aeroplanes from H.M.S. "Hermes" were placed at the disposal of the relief authorities.
- 63. In order to provide food for the famine-stricken population, the Chinese Government arranged with the Federal Farm Board for the purchase at current market prices of 450,000 tons of wheat from America. Under the terms of the agreement the buyer paid for the wheat and/or flour tendered by delivering to the designated agent of the seller obligations of the Chinese National Govern-

ment bearing the same date as that of the ocean bills of lading covering each shipment. Such obligations were payable both as to principal and interest at New York in United States gold dollars. The obligations bore interest at the rate of 4 per cent. per annum, payable on the 30th June and the 31st December of each year, and one-third to mature the 31st December, 1934, one-third thereof to mature the 31st December, 1935, and one-third to mature the 31st December, 1936. The money in payment of this loan is to be raised by the Chinese Government as shown in the Finance Section of this report. Endless difficulties were encountered in the handling of the shipments of wheat and their disposal and in the prevention of pilferage, and it would not be unfair to say that the wheat deal seemed to have been engineered by interested parties with very little regard for the difficulties which lay in the way of distribution once the wheat had arrived in the country.

64. When the floods began to subside at the beginning of September the danger of attacks on British lives and property by Communist bands and refugees became a live issue, and the Chinese Government were accordingly requested to take all precautions to forestall possible trouble. This they did by sending extra troops to Hankow. No epidemics on any large scale occurred.

(6) Military Operations.

(a) General.

- 65. The closing months of 1930 found Chiang Kai-shek, President and Commander-in-chief, at the zenith of his power. After a protracted struggle, he had successfully defeated his most dangerous enemies, Yen and Feng; there only remained the Communist menace to be dealt with once and for all.
- 66. Some headway had been made towards curbing the activities of the unruly and subversive in Kiangsi, but nothing decisive has yet been undertaken against bandit armies. Slowly but surely the Communist bandits threatened to gain possession of the whole of the Yangtze Valley; the time had come when something had to be done.
- 67. Chiang Kai-shek signalised his return to Nanking by declaring he would not rest till all the undesirable elements in the country were completely exterminated.
- 68. This he set out to do. He might have accomplished something had his plans not been upset by the Canton clique, who, scenting the right moment to create trouble, initiated, during the early part of May, a state of "deferred war" along the Kwangtung-Hunan frontier.
- 69. In July another revolt in the north broke out which also served to deflect Chiang Kai-shek from his task against the Communists.
- 70. Shih Yu-san, who since the defeat of Yen and Feng had been a "disturber of unity" in South Hopei, advanced northwards along the Pei-Han Railway threatening Peking.
- 71. Chang Hsueh-liang, as Chiang Kai-shek's co-partner in keeping the peace in North China, met and defeated him in battle near Paoting-fu. Shih fled to Dairen, and once more the air cleared. The respite was short, a strained Sino-Japanese atmosphere in Manchuria became actual conflict.
- 72. On the night of the 18th-19th September Japanese railway protection troops, asserting that Chinese soldiers had damaged the tracks of the South Manchurian Railway, seized Mukden. The end of the year found Japan to all intents and purposes in complete possession of Manchuria.
 - 73. The outstanding events of military importance during the year were-

(a) Chiang Kai-shek's anti-bandit campaign.

(b) The Canton rebellion.(c) Shih Yu-san rebellion.

(d) The Sino-Japanese conflict in Manchuria.

(b) Communist-Bandit Suppression Campaign.

- 74. Ho Ying-chin, War Minister and Chiang's trusted lieutenant, had, with limited troops at his disposal, spent many months attempting to destroy bandits in Kiangsi, but had been able to do little more than hold his own against people who employed guerilla tactics, a form of warfare the Chinese soldier does not at all relish.
- 75. The campaign, as far as it went, before more pressing events disturbed Chiang Kai-shek, may be divided into four periods:—

First Period: January 1931.

- 76. The Government had eleven divisions concentrated at various strategical points in Kiangsi. This force of about 100,000 men was opposed by almost an equal number of bandits, according to official reports given out at the time at Nanking.
- 77. There was little or no real fighting. The period was characterised by the heavy reverses suffered by the 18th and 50th Government Divisions. Both these units were badly defeated, their arms being seized by the bandits.

Second Period: February to June 1931.

- 78. Ho Ying-chin, under mandate from the Commander-in-chief, returned to Kiangsi, with headquarters at Nancheng.
- 79. Nine divisions as reinforcements were despatched to the province, suggesting that at last serious attempts were to be made to grapple with the bandit menace. By the middle of March these units, including three divisions, former Feng Yu-hsiang troops, under Sien Lien-chung, had reached their designated areas and an offensive on all fronts was ordered. The Government troops advanced slowly, every precaution being taken to guard against surprise by the enemy.
- 80. Precautions notwithstanding, this period, like the first, was not without its regrettable incidents. The bandits scored several victories against individual divisions, disarmed them and took prisoners. The bandits, however, showed signs of shifting their ground and began a move southward in the province.

Third Period: June to September 1931.

- 81. Chiang Kai-shek proceeded to Kiangsi and took over command on the 21st June. His presence as the conqueror of Yen and Feng infused new life into the troops and galvanised the lesser commanders into some semblance of activity. He had several regimental commanders shot for losing their units, and generally showed the army he meant business. More divisions were transported from other provinces, bringing the total of Government troops now at the front to over 200,000 men with a dozen aeroplanes.
- 82. In July the army achieved a great victory over the bandits. They lost many of their strongholds, including Lungkan, Huangpi, Ningtu and Tungku, which had long been the main headquarters of the Communist movement in Kiangsi. Government headquarters reported the capture of 30,000 prisoners and over 14,000 rifles. This was undoubtedly a big set-back to the bandits, who now retreated to Jui-cheng, on the Fukien border.
- 83. Unfortunately for Chiang, just as he had established this ascendancy the Canton clique, who had by this time become blatant in their demands at Nanking, started to move troops towards the Hunan border. The bandits saw in this action the arrival of new allies on the scene, and Chiang was forced to detach troops to meet the threat.
- 84. On the top of this came the Japanese stroke against Mukden, which brings us to the Fourth Period, during which the offensive was called off.

Fourth Period: October to December 1931.

85. The confused political situation and the shock created at Nanking by the taking of Mukden on the 18th September, by the Japanese, brought

Chiang Kai-shek hurrying back to Nanking. The Kwangtung divisions operating in South Kiangsi were brought to Nanking as a token to the Canton politicians that they could safely come to Nanking. Gradually it came to be understood that the bandits, in face of the new common danger from outside, were now prepared to co-operate with Nanking, and the offensive gradually died away. This led to fraternisation and tacit agreements on the part of the troops and bandits not to fight each other.

- 86. In December over 5,000 of Sien Lien-chung's men (former Feng Yu-hsiang troops), in the absence of their immediate commander, suddenly went over to the bandits, thus undoing to a great extent the good work Chiang Kai-shek had already put in towards relieving Kiangsi from the Communist menace.
- 87. The year closed with twelve divisions still in the province with the idea of keeping the bandits in check; a situation which will surely lead to the turnover of more dissatisfied Government troops, whose pay is always something like two to three months in arrears. At the moment (the 1st January, 1932) the Communist-bandit armies show signs of a renewed activity, due no doubt to the encouragement they derive from wholesale chaotic conditions throughout the country and the pusillanimous antics of the Canton clique at Nanking.

(c) Canton Rebellion.

- 88. In early May Canton, where political elements had for some time been plotting to force Chiang Kai-shek's resignation, declared independence and started a state of "deferred war" along the Kwangtung-Hunan frontier. A circular telegram was issued denouncing Chiang Kai-shek and demanding his resignation within forty-eight hours. Circulars announced the formation of an independent Government, and plans were formulated for the invasion of Hunan, including the capture of Changsha and the occupation of the bandit-ridden province of Kiangsi.
- 89. Chiang, stating he had no intention of fighting the rebellion, which was disgraceful in view of the Communistic threat to the whole country, proceeded with his concentration in Kiangsi. As a precaution, however, he sent the 48th Division from Hupeh to South Hunan as reinforcements to Ho-chien's (chairman of Hunan) regular divisions, which were already in touch with the advanced elements of the Cantonese armies.
- 90. Bickerings and divided opinions amongst the Kwangtung and Kiangsi military leaders now caused a withdrawal of the troops of both provinces within their respective boundaries and a period of mutual suspicion set in. After much talk amongst the politicians things were patched up sufficiently to permit of a second plan of invasion northwards being announced. A rebellion (referred to under another heading) started by Shih Yu-san in the North fixed a date for a simultaneous advance by the combined armies into Hunan and Kiangsi. Ho-chien's troops were to turn over, and it was expected that many Government divisions would refuse to fight. Ho-chien soon showed his real attitude by calling for reinforcements from Nanking and ordering his troops to resist the invaders. This served to damp the ardour of the invaders, who again withdrew their advanced troops.
- 91. In September Kiangsi and Kwangtung troops again crossed their frontiers, preceded by the usual slogans on the part of the politicians that Chiang must go. In reply Chiang despatched five divisions to Hunan, and to all appearances fighting was inevitable. Reaction to the Japanese stroke at Mukden served to postpone again another useless war.
- 92. Unity in face of the common danger now became the national slogan, and Chiang invited the Canton politicians to Nanking to discuss peace. The year closed with the politicians of both sides wrangling for places in the new Government. Chiang has temporarily left the arena, but retains his army wherewith to impose his will on his opponents at some later date.

(d) Shih Yu-san's Rebellion.

93. Shih Yu-san was formerly one, if not the most important, of the Kuominchun secondary leaders. He fell out with Feng, and at once assumed [7371]

the rôle of a war lord at the disposal of the highest bidder. His record for the two years ending July 1931, when he revolted and attacked towards Peking, was continuously one of duplicity and chicanery—typical of the civil commotion war lord at his best.

- 94. Shih, realising that he was thoroughly suspect, and the first for elimination by either Chiang Kai-shek or Chang Hsueh-liang, decided he must act at once or he would be too late. The Canton rebellion, Communist situation in Kiangsi and the probability that Han Fu-chu and one or other Northern recalcitrants might join his revolt decided him to have a go against Manchurian troops, for whom he had little respect as fighters.
- 95. On the 15th July Shih made his lightning stroke, seized such rolling-stock as was within his reach on the Pei-Han Railway and prepared to advance northward up the line. He had at his disposal 60,000 men in all as opposed to 80,000 which Manchuria had at their immediate disposal. His attack made some progress in its early stages, but it was clear from the outset that, unless the allies, whom he expected would come to his aid, declared themselves, the attempt would fail. Manchuria also had at their disposal some thirty aeroplanes. These machines, though badly handled, went some way towards lowering the moral of Shih's men, who had no anti-aircraft weapons of any sort.
- 96. The rebellion was short-lived. After his first effort to penetrate the Manchurian defence, Shih Yu-san fled, leaving most of his troops to shift the best way they could for themselves. Shih himself is now (January 1932) in Shantung under the protecting wing of his quondam ally Han Fu-chu.

(e) Sino-Japanese Conflict in Manchuria.

- 97. On the night of the 18th–19th September Japanese railway troops, asserting that Chinese soldiers had damaged the tracks of the South Manchurian Railway, carried out a series of rounding-up affairs terminating in the complete possession of Mukden, and other important strategical points in Manchuria.
- 98. During a short period of twelve hours on the 18th–19th, the Japanese took complete possession of Peitai-ying (North Barracks), the arsenals and the aerodrome at Mukden. There was some fighting at Chang-chun (north terminus of South Manchurian Railway) the same morning. Here the Japanese met some disorganised resistance from the Kirin troops occupying the barracks. but this was speedily overcome.
- 99. Kirin city was occupied on the 21st September, Tunhua, the eastern terminus of the Kirin-Tunhua Railway, was taken over the next day. This put the Japanese in complete control of the much discussed Chientao region through which the important strategical link completing through rail communication from the Korean frontier to North-West Manchuria is destined to run.
- 100. Occupation of one or more strategical and economically important points on Chinese railways completed the chapter of Japanese occupation of South Manchuria, with the exception of the Peking-Mukden Railway zone.
- 101. The situation then stabilised for a period. The Government at Tokyo were, however, kept busy making excuses to the world at large while their military consolidated and put in hand such preparatory steps as they considered necessary towards the gradual taking over of all Manchuria.
- 102. With Mukden and Kirin safely in their hands, and a friendly local Government established at each place, there still remained Tsitsihar, the capital of the Heilungkiang Province as a final objective. True, the Chinese had set up a provisional local Government of Liaoning Province at Chinchow, but they were only a Government in name and could be safely left to a later date to be dealt with.
- 103. From a military aspect the problem of Tsitsihar was easy in spite of shortage of men and guns. The real question was how to encompass the fall of Tsitsihar without unnecessarily attracting the attention of the League. The Japanese decided to use one Chang Hui-peng, who had some 3,000 ill-trained levies at his disposal, to turn out General Ma Chan-shan, whose troops, astride the Taonan-Angangchi Railway, barred the way to Tsitsihar. They provided him with rifles and ammunition, gave him free advice and promised him support

should he reach Tsitsihar. Chang's failure to come up to expectations forced the Japanese to take on the business themselves. This led to the battle of the Nonni River, where, after some delay while reinforcements were brought up, the Japanese defeated and drove General Ma and his army of nearly 10,000 men north towards Koshan and Hailun (north of Harbin).

- 104. The conclusion of operations towards Tsitsihar freed the army for its next move towards Chinchow.
- 105. Chinchow was bombed from the air on the 8th October with the idea that the embryo provisional Government would withdraw. The raid was a failure, it drew international attention to the Manchurian situation, stiffened the attitude of the Chinese officials, and gave the troops already in the area time to reconsider the ignominious rôle they were called upon to play at Mukden on the 18th September.
- 106. Two months elapsed before Japan found herself in possession of Chinchow. The intervening period was occupied by reconnaissances in force towards Chinchow, threats to the Chinese communications by landings and feints at Tientsin and Shanhaikuan, and "friendly" exhortations to get out before the blow fell.
- 107. On the 21st December, the Japanese started "clean up" operations against bandits in areas contiguous to the forward zone occupied by the Chinese troops based on Chinchow. The 20th and 2nd Divisions advanced along the main Peking–Mukden Railway system from Hsinmintun and the Yingkow branch line respectively; their flanks being secured by detachments sent out to break up bandit nests as found convenient. On the 31st December, the advanced troops of these divisions met at Koupangtze, the Chinese armoured trains and troops stationed east of the Ta-ling River having safely withdrawn across the river during the previous twenty-four hours.
- 108. It is almost certain that the Japanese would have been forced to halt on the line of the Ta-ling river in order to review the situation had not the Chinese anticipated events by ordering a general retreat on the night of the 28th. Japanese vanguards entered Chinchow on the 2nd January, followed by the head-quarters of the 20th Division on the morning of the 3rd. The remaining portion of the Peking–Mukden Railway as far as Wu-chia-tun, the first station outside the Wall, was occupied during the course of the next few days.
- 109. This completed Honjo's immediate task. The last of Chang Hsueh-liang's own troops have been expelled from Manchuria. There only remains Jehol Province and a few isolated trade marts, such as Harbin, to be dealt with.

II.—FOREIGN RELATIONS.

(1) Extra-territoriality.

- 110. The position in regard to the extra-territoriality negotiations at the beginning of the year 1931 was as follows: Following on the exchange of formal correspondence in 1929, and the opening of preliminary discussions in the early part of the year 1930, the proposals of His Majesty's Government in the United Kingdom for the gradual abolition of British extra-territorial rights in China had been communicated to the Chinese Government on the 11th Setember, 1930. To these proposals the Chinese Government had replied by putting in, in turn, on the 1st December, 1930, a counter-draft, which omitted the four major safeguards contained in the British proposals (evocation, foreign co-judges, reservation of criminal jurisdiction, and exclusion of certain areas), and also deleted or emasculated the greater part of the more detailed minor safeguards concerning matters such as guarantees in regard to taxation, the operation of the Chinese courts, limitation of police jurisdiction, arrest, domiciliary visits, rights in immovable property, expropriation, immunity of shipping, arbitration, rights of business organisations, discrimination, and so on.
- 111. The Chinese counter-proposals, and His Majesty's Minister's comments and request for instructions thereon, had reached the Foreign Office [7371]

early in January 1931, and the next few weeks were occupied by their study in London and by consultation with the American Government. The latter, as the result of their examination of the Chinese counter-proposals submitted in December, had formulated and communicated to His Majesty's Government in the United Kingdom in January a new draft, the principal features of which had been the dropping of evocation and foreign co-judges. As the result of discussions between London and Washington, the State Department subsequently withdrew this draft, and on the 7th February they submitted to the Chinese Minister in Washington a statement intended to indicate the nature of the concessions they were willing to make. In this document no mention was made of the question of foreign co-judges, but evocation was definitely abandoned. this statement the Chinese Government had replied on the 20th February expressing their appreciation of the concessions offered, but repeating their expressing their appreciation of the concessions officed, inability to accept any of the three remaining major safeguards, namely, foreign inability to accept any of criminal jurisdiction, and excluded areas. The State Department thereupon took no further action for the time being and intimated that they would await further developments with special reference to His Majesty's Minister's impending negotiations at Nanking.

- 112. In accordance with his instructions, His Majesty's Minister arrived in Nanking on the 1st March for the purpose of opening the negotiations. On the 7th March Sir Miles Lampson received the further detailed instructions for which he had been waiting. These were, in brief, to the effect that rights of evocation, the reservation of criminal jurisdiction and foreign co-judges should, as and when necessary, be progressively abandoned, in return for the retention of the other safeguards which were regarded by His Majesty's Government in the United Kingdom as vital, namely, the reservation of certain treaty port areas, with special reference in the last resort to the International Settlement at Shanghai, adequate arrangements in regard to the functions of the legal advisers, and satisfactory guarantees and assurances in connexion with taxation, titles to real property, expropriation, domiciliary visits, immunity of shipping, rights of business organisations, discrimination, and other minor points.
- His Majesty's Minister opened the negotiations with the Minister for Foreign Affairs on the 8th March, beginning with a discussion of the four major safeguards—evocation, foreign co-judges, criminal jurisdiction and excluded areas. As was to be expected, a deadlock was soon reached. His Majesty's Minister then suggested as an alternative method of approach that the many so-called minor safeguards, to which His Majesty's Government in the United Kingdom attached the greatest importance, should be first discussed, and he gradually developed the argument that, if it was found possible to secure complete satisfaction in regard to these legal safeguards, it might influence the attitude of His Majesty's Government towards the whole settlement, including the question of the reservation of criminal jurisdiction. Eventually Dr. Wang agreed, with some reluctance, to trying this new line of approach, and it was decided that as the next step the respective experts on each side, Mr. Teichman and Mr. Hsu Mo, should meet and see how far they could work out from the British and Chinese proposals, which were at that time poles apart, an agreed composite draft in regard to the legal safeguards without touching for the moment on the four major points of principle in dispute. In this way an important tactical advantage was gained at the outset in these complicated and difficult negotiations; that is to say, that His Majesty's Minister was able to build on a gradually broadening basis of common ground in regard to the less contentious points from the bottom up, instead of dealing with the problem the other way round and being forced to give way at the outset on the major issues.
- 114. In the meanwhile the other interested Powers had followed the lead of His Majesty's Government in the United Kingdom and the American Government in initiating negotiations with the Chinese Government. On the 12th March the Japanese Chargé d'Affaires presented the Japanese proposals, which were, as was expected, of a very conservative nature. (It will be recalled that the Chinese contention was that Japan's treaty rights had already expired.) About the same time the French Minister put in his proposals, which were along the lines of the British and American plans of the previous autumn, omitting, however, evocation and some of the detailed legal safeguards. Apart from Great

Britain, the United States and France, and excluding Brazil, with whom no negotiations appeared to be contemplated, there remained of the Powers still with their extra-territorial rights theoretically unimpaired only Norway and Holland; and it now transpired that both the Norwegian and Netherlands representatives in China were seeking a settlement along the lines of the Belgian, Portuguese, Spanish, Danish and Italian precedents, that is to say, abandoning more or less unconditionally their extra-territorial rights as soon as the other Powers had done so. As regards the American Government, the extent to which they were conducting their negotiations in Washington or in Nanking was never entirely clear. Hs Majesty's Minister kept, however, in the closest touch with his United States colleague, informing him of all the proposals put forward, consulting him at every turn, and communicating to him copies of the agreed texts as they were arrived at. In this way, while Mr. Johnson did not himself conduct any negotiations direct with the Minister for Foreign Affairs, the American Government were able to adopt, as His Majesty's Minister's negotiations proceeded, the results which were obtained

115. The detailed negotiations regarding the legal safeguards between Mr. Hsu Mo and Mr. Teichman opened on the 12th March, and at the same time His Majesty's Minister was able to put before the Minister for Foreign Affairs certain alternative proposals for strengthening the position and functions of the foreign legal counsellors to be attached to the special courts hearing foreign cases in return for the abandonment of the idea of foreign co-judges, which, it was quite evident, the Chinese Government were unable to entertain. As the result of three days' work, good progress was made on certain of the less contentious legal safeguards, and on the 14th March His Majesty's Minister was able to report by telegraph the texts of a number of articles which had been tentatively agreed upon. In the meanwhile Sir Miles Lampson took the opportunity, while awaiting his instructions, to suspend discussions for a few days in order to pay a visit to Shanghai and explain to the Joint Committee of the British Chamber of Commerce and China Association the course of and the position reached in the negotiations.

His Majesty's Minister returned to Nanking on the 23rd March and resumed his discussions with Dr. Wang a day or two later. Once again, by referring the detailed work to a sub-committee of experts, good progress was made, and on the 27th March Sir Miles Lampson was able to submit by telegraph, just under three weeks from the opening of the negotiations on the 8th March, agreed texts of articles and attached documents covering more than half of the body of the proposed treaty in connexion with the legal safeguards. At this point it seemed desirable to allow a pause in the negotiations to give time for both sides to take stock of the situation, and His Majesty's Minister accordingly arranged to return to Peking over the Easter holidays. Before doing so, however, he decided that the time had come to get to closer grips with the main issues and to sound the Minister for Foreign Affairs in regard to the possibility of trading criminal jurisdiction in return for satisfactory arrangements as regards the "reserved areas." This Sir Miles Lampson was able to do at a private interview with the Minister for Foreign Affairs on the 30th March. Dr. Wang's reply was to explain why it was utterly impossible for his Government to give way over the four reserved areas (Shanghai, Tientsin, Canton and Hankow), but he eventually offered to propose to his Government the reservation of the International Settlement at Shanghai for a brief period. His Majesty's Minister was unable to consider so inadequate a proposal, and the position was left at that for the time being, namely, that he (Sir Miles Lampson) had offered to recommend to His Majesty's Government in the United Kingdom the surrender of criminal jurisdiction in return for the four reserved areas.

117. In the meantime a new factor had been introduced into the situation by the approach of the People's Convention, which was to open at Nanking on the 5th May, and the insistence on the part of the Chinese Government that something would have to be accomplished in connexion with the extraterritoriality negotiations before that date. On the 10th April the Minister for Foreign Affairs had issued a declaration in the form of a speech to the press on the subject of the negotiations. In this declaration Dr. Wang admitted that

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good progress had been made in the negotiations, especially with Great Britain. Unfortunately, certain vital points were still outstanding, disagreement over which might render the negotiations abortive. The Chinese Government and the Chinese people would, however, brook no further delay. The People's Convention was to meet on the 5th May. Consequently, both Government and people were asking what would be accomplished by then in connexion with the abolition of the unequal treaties, as laid down by Dr. Sun Yat-sen in his death-bed behest. It was the earnest hope of the Chinese Government and people that Great Britain and the United States, as well as the other Powers concerned, would "courageously seize fleeting time by the forelock and co-operate with the Nationalist Government in consummating the abolition of extra-territoriality, the bulwark of the unequal treaties." Dr. Wang concluded with the statement that, unless the solution desired by China was completely in sight, he and his colleagues would be constrained to "declare the present negotiations with the Powers concerned as deadlocked." The attitude of the Chinese Government at this time was that it was essential for them to be able to present themselves before the People's Convention on the 5th May with something definite to show in connexion with the abolition of extra-territoriality. Already, once before, they had played to the popular gallery by unilaterally declaring extra-territoriality at an end on the 1st January, 1930. This declaration had remained a mere paper gesture, a position they had explained by letting it be understood that the necessary agreements to give effect to it would immediately be negotiated with the Powers concerned. Nearly a year and a half had, however, since passed and nothing had happened. If, therefore, they could show no result in their negotiations by the time the People's Convention met on the 5th May, they would be compelled to take some decisive step.

His Majesty's Minister had left Nanking on the 2nd April and remained in Peking over Easter for some ten days, awaiting the comments and instructions of His Majesty's Government in the United Kingdom on the texts of the articles provisionally agreed upon and on certain of the outstanding points. Having received his instructions, Sir Miles Lampson left Peking on the 16th April, and on the same day, breaking his journey at Tientsin, met the local Joint Committee of the British Chamber of Commerce and China Association, and explained to them also the course of, and the position reached in, the negotiations. Sir Miles Lampson arrived back in Nanking on the 18th April and resumed his negotiations with the Minister for Foreign Affairs on the same day, Mr. Teichman having proceeded a few days ahead to carry on his detailed discussions with Mr. Hsu Mo. After this sitting on the 18th April, Sir Miles Lampson had a further private conversation with Dr. Wang with the object of sounding him again in regard to the reserved areas, but without result. Dr. Wang repeated his offer of the exclusion of the International Settlement at Shanghai for a limited period, and reiterated the impossibility of his Government agreeing to anything more. As the result of these discussions, however, the actual treaty itself began to take shape. On the 27th April His Majesty's Minister was able to reach more or less definite agreement on some thirteen articles of the proposed treaty and attached documents covering the transfer of jurisdiction, the establishment of special courts, the functions of the foreign legal councillors, the rights of foreign lawyers, taxation, arbitration, rights in immovable property, immunity of premises, military requisitions and forced loans, shipping immunities, rights of companies, handling of pending cases, and non-discriminatory treatment. Detailed consideration of the question of legal safeguards in connexion with criminal jurisdiction (arrests, trial, bail, imprisonment, and so on) had been deferred pending further developments in the negotiations, but these points were satisfactorily disposed of later on. Apart from the above, there now remained outstanding only a few of the more contentious items, including the complicated and troublesome question of personal status cases, as well as that of the reserved areas, which had become the crucial point on which the fate of the negotiations depended. On the 27th April His Majesty's Minister had a further private conversation with the Minister for Foreign Affairs without, however, being able to induce Dr. Wang to improve on his former proposal, which he now put forward as a definite and final offer, namely, the exclusion of the International Settlement at Shanghai for a period of three years, an offer which Sir Miles Lampson again declined to discuss.

119. In the meantime the position had not been improved by the Norwegian and Netherlands Ministers concluding their negotiations and joining the majority by signing agreements on the models of those concluded in 1928 with Italy, Spain, Denmark, Portugal and Belgium.

120. On the 29th April His Majesty's Minister received telegraphic instructions dealing generally with the question of the reserved areas, and specifically with Dr. Wang's offer of the exclusion of the International Settlement at Shanghai for a period of three years, which was definitely unacceptable to His Majesty's Government in the United Kingdom. His Majesty's Minister was further instructed to suggest to the Chinese Government that they should accept the reservation of the four areas, and that provision should be made for a joint Sino-British commission to study the question of the settlements and concessions, on the understanding that negotiations on the basis of the recommendations of this commission would be entered into within a period of three or five years. On the 1st May Sir Miles Lampson communicated the substance of these instructions to Dr. Wang, who repeated, however, in the most categoric terms, that it was absolutely impossible for his Government to meet His Majesty's Government over the four reserved areas, and refused to consider the proposals for a joint commission.

121. In the meantime there had been sudden and unexpected developments in the political situation in China. On the very eve of the assembling of the People's Convention on the 5th May, the military and political leaders at Canton had issued a declaration openly repudiating General Chiang Kai-shek and challenging the authority of the Nanking Government. It was impossible to tell how serious this Canton movement might turn out to be, but in the circumstances the only practical course to follow was to continue the negotiations as though nothing had happened pending developments, and further indications of the attitude and position in the country of the National Government.

122. The People's Convention opened on the 5th May, and at the same time the Nationalist Government took their much heralded "unilateral action" by issuing a mandate on the subject of foreign extra-territorial rights. The mandate promulgated a set of regulations in twelve articles to come into force on the 1st January, 1932, governing the exercise of jurisdiction over foreign nationals As was expected, these regulations were designed to set up the framework of the arrangements agreed upon in the negotiations, including special courts and legal counsellors, and provided for the substance in emasculated form of the agreed assurances and legal safeguards. At the same time the Minister for Foreign Affairs issued a statement in which he referred to the mandate of the 28th December, 1929, in pursuance of the above pronouncement the National Government had been continuing negotiations with the Governments of the six Powers concerned during the past year and a half; certain of these Governments had concluded satisfactory arrangements; but the negotiations with the other Powers, including Great Britain and the United States, had not yet yielded the desired solution; the National Government appreciated the warm sympathy already shown by these Powers, especially Great Britain, in its endeavours to consummate China's aspirations, and it was sincerely to be regretted that they did not see their way to meet completely the ardent wishes of the Chinese Government and people; the National Government had now no alternative, but to declare that the extra-territoriality negotiations with the various Powers had reached an impasse, and to issue the mandate concerning the exercise of jurisdiction over foreign nationals in China, to come into force on the 1st January, 1932.

123. The negotiations were resumed on the 8th May without reference to the issue of the mandate, and good progress continued to be made on various outstanding points. On the 12th May, while awaiting instructions on the recent work, His Majesty's Minister proceeded to Shanghai in order to take the opportunity of keeping the local Joint Committee of the British Chamber of Commerce and China Association informed of the position reached in the negotiations. His Majesty's Minister arrived back in Nanking on the 18th May, and on the same afternoon was once more in session with the Minister for Foreign Affairs. There were now left outstanding only the preamble of the proposed treaty, the question of the reserved areas, and the provisions regarding duration

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and ratification. After hammering out some progress on the two latter points, His Majesty's Minister raised the major outstanding issue of the reserved areas and presented a new draft article providing for the exclusion of the four areas and for a joint commission to study the question of these areas and for negotiations on the basis of the recommendations of such commission to be entered upon within a certain number of years. As was expected, the Minister for Foreign Affairs again refused to consider this proposition, and no progress was made.

- The next few days were occupied in disposing of the other outstanding points in the draft treaty. points in the draft treaty. During this period, from the 21st May to the 26th May, His Majesty's Minister was in constant negotiation with the Minister for Foreign Affairs, both officially and privately, on the subject of the reserved areas, with the result that Dr. Wang, who had already been induced to improve on his original offer of the exclusion of the International Settlement to the extent of proposing the exclusion of the whole area of Greater Shanghai, a very important concession, was finally and with the greatest difficulty, screwed up to considering the reservation of this Shanghai area for a maximum period of ten years and of an area at Tientsin for five. It was by now, in view of the complications developing in the internal political situation, becoming increasingly desirable that the negotiations should be wound up as soon as possible and the whole question left in abeyance pending the outcome of the conflict between Nanking and Canton. At the same time it was equally desirable that some means should be found of clinching as far as possible the bargain in respect of the agreed texts of the draft treaty, while allowing of the necessary degree of elasticity to enable His Majesty's Government in the United Kingdom to sit back and await the outcome of the internal political crisis. To meet this situation it was finally decided that copies of the draft treaty and attached documents should be exchanged between His Majesty's Minister and the Minister for Foreign Affairs in covering letters stating that the texts were being referred for confirmation to their respective Governments. This was accordingly done, on the 6th June; and thus, after almost exactly three months of intensive negotiation, an agreement, ad referendum had been reached, but with the crucial article concerning the reserved areas not finally disposed of on either side.
- 125. In view of the trouble which now developed between the National Government and the Canton faction, no further developments occurred in connexion with the negotiations during the summer. In the middle of September, however, just before the Japanese action in Manchuria introduced a new complication, the American Minister informed His Majesty's Minister that he had received a personal letter from the Minister for Foreign Affairs expressing the earnest hope that he, Mr. Johnson, would visit Nanking to take up on behalf of his Government the extra-territoriality negotiations, regarding which the time available was rapidly running out, referring to the date, the 1st January, 1932, fixed by the Chinese Government for the enforcement of the regulations taking the jurisdiction over of all foreign nationals in China. Mr. Johnson went on to say that he felt it difficult to ignore this request, and that his inclination was to proceed to Nanking and enter into the negotiations as desired by Dr. Wang. A day or two later, however, there occurred the Japanese coup in Manchuria which put a new complexion on the whole situation and drove the question of extraterritoriality out of the minds of the Chinese.
- 126. Nothing more happened in connexion with the negotiations until the middle of November, when His Majesty's Minister was in Nanking in connexion with the Sino-Japanese crisis. In the meanwhile Dr. Wang had resigned. On the 12th November His Majesty's Minister found an opportunity of broaching the question of the extra-territoriality mandate informally with the Acting Minister for Foreign Affairs, Mr. Lee, and pointing out that any attempt to bring it into force on the 1st January would provoke immediate international complications. His Majesty's Minster was also able to make the point that China was now, in connexion with her dispute with Japan, loud in her support of international law and the Covenant of the League of Nations, and that she might find it awkward if, after her attitude in the Manchurian question, she was called before the League on account of any attempts at the unilateral abrogation of foreign treaty rights in regard to extra-territoriality. Mr. Lee said he was well aware that the mandate could not be brought into force on the 1st January, and

added that the only question now was how to bring about its postponement without prejudice to the position of the National Government in connexion with the international situation. A fortnight later His Majesty's Minister had an opportunity of mentioning the matter of the mandate informally to Dr. Koo, who was about to take up the post of Minister for Foreign Affairs, and of suggesting that the question of its postponement should be one of the first matters which Dr. Koo should consider on assuming office. As the time was now rapidly running out, His Majesty's Minister referred the position once more to His Majesty's Secretary of State for instructions, and suggested that it might be well that he should without further delay take the matter up officially and give the Chinese Government to understand that His Majesty's Government could not recognise any impairment of British extra-territoriality rights on the 1st January or until such time as an agreement mutually satisfactory had been reached. The Secretary of State's instructions were received in the middle of December. His Majesty's Minister was informed that His Majesty's new Government in the United Kingdom had now considered the question of extra-territoriality in the light of recent developments. By winding up the negotiations in June last His Majesty's late Government had secured a strong tactical position from which to face any new situation that might arise during the period of political chaos that, as was then foreseen, lay ahead. His Majesty's Government in the United Kingdom considered that the negotiations had been carried to the furthest possible point, and that the whole question would now have to remain in abeyance until the negotiations of the other Powers had made similar progress and until there seemed some probability that China would be able to implement any treaty that might result from such negotiations. As regards the mandate of the 4th May, His Majesty's Minister was instructed to take an early opportunity of stating to the Minister for Foreign Affairs that His Majesty's Government would prefer entirely to ignore the mandate, and did not, therefore, demand its cancellation. They would, however, take a most serious view of any attempt to enforce the mandate on the 1st January or, indeed, at any time before the negotiations on the subject of extra-territoriality had been brought to a satisfactory conclusion and an agreement had come into force. Any such attempt would be firmly resisted, and His Majesty's Government in the United Kingdom would not hesitate to take what measures were open to them to maintain the treaty privileges of their nationals.

127. His Majesty's Minister was by this time back in Peking, and he accordingly instructed Mr. Ingram, who was acting as his representative at Nanking, to make to the Minister for Foreign Affairs a verbal communication in his name on behalf of His Majesty's Government in the United Kingdom in the above sense. Mr. Ingram was to do this in a friendly but formal way, leaving no doubt as to the seriousness of the warning, which, however, was not intended as a threat, but rather as a helpful indication in advance of the serious consequences of any attempt to enforce the mandate of the 4th May. Mr. Ingram delivered this message on the 28th December to Mr. Hsu Mo, representing the Minister for Foreign Affairs. Mr. Hsu Mo stated that the Waichiaopu had suggested to the National Government a method of harmonising the mandate with the existing state of affairs, and that he felt confident that the fears of His Majesty's Government of unilateral action by the Chinese Government would prove unfounded. On the 29th December a further mandate was, in fact, issued by the National Government postponing the enforcement of the mandate and regulations of the 4th May. This mandate stated that, owing to calamities and trouble in the various parts of the country, it had not been possible to complete the necessary arrangements for putting the new regulations into operation, and they were therefore temporarily postponed; the authorities concerned were, however, ordered to complete these arrangements as soon as possible in order that a date might be fixed to bring into effect the provisions in question. On the 31st December His Majesty's Minister issued circular instructions to His Majesty's consuls in China explaining for their information and guidance the position in connexion with the extra-territoriality negotiations. After recalling the history of the negotiations, which had resulted in June in a draft treaty being referred to His Majesty's Government and the Chinese Government for their consideration, and in their subsequent suspension owing to the political situation in China, Sir Miles Lampson informed His Majesty's consuls of the

warning recently conveyed to the Chinese Government by His Majesty's Government in the United Kingdom. Since this warning had been addressed to them the Chinese Government had issued on the 29th December their further mandate postponing the enforcement of the regulations of the 4th May. It was not, therefore, anticipated that any serious attempt would be made on the Chinese side to force the pace in the immediate future, but His Majesty's consuls were reminded of Sir Miles Lampson's circular instructions issued in January 1930, the terms of which still held good.

(2) United Kingdom.

(a) General.

- 128. As far as Sino-British relations are concerned, the main event has been the gradual progress made in negotiations with the Chinese Government in the matter of the abolition of British extra-territorial rights in China. As this question is dealt with fully in a separate section of the report, suffice it to say that the negotiations continued almost uninterruptedly from the beginning of the year until June, when a draft treaty was prepared for reference to and consideration by the United Kingdom and Chinese Governments. Since that date, owing to internal disturbances in China and the events in Manchuria, no further progress has been made. Representative bodies of the British communities at Shanghai and Tientsin were kept informed of the course of the negotiations, and, as was to be expected, the future of the treaty port areas, under the provisions of the draft treaty, was the subject of much speculation and criticism.
- 129. Although relations with China have, on the whole, been satisfactory throughout the year, the diplomatic horizon was for some time somewhat darkened by the inability of the Chinese Government to deal satisfactorily and expeditiously with the Thorburn case and the Hankow assault incident. The cordiality of Sino-British relations was at one moment gravely threatened, and public indignation, both in China and elsewhere, rose to fever heat. The original circumstances of the case, which are described separately, naturally receded into the background, and the incidents were used as a lever to secure strong action by His Majesty's Government in China and as proof that any safeguards or guarantees offered by the Chinese Government in connexion with the extraterritoriality negotiations were practically worthless.
- 130. The absence of any real control or authority on the part of the Central Government in regions outside the immediate vicinity of the capital and important centres, has given rise to frequent difficulties in the matter of the settlement of outstanding cases and the proper protection of British interests. On the Middle Yangtze bandit activities and firing on British ships assumed serious proportions at the beginning of the year, so that it was found necessary to draw the attention of the Chinese Government to this unsatisfactory situation, which was aggravated by the removal of navigation marks. A proposal that wireless installations should be fitted to British ships to circumvent any danger did not, unfortunately, commend itself to the shipping companies. The boycott of British shipping at Ichang, Wanhsien and Changsha still continued intermittently owing to the attitude of the local authorities or labour unions, but, with the advent of the anti-Japanese boycott at the end of the year, the situation materially improved.
- 131. Owing to the unsettled state of the country the position of missionaries in the interior has by no means been free from danger. Father Tierney, who was captured by bandits at the end of 1930, died in captivity in March, in spite of urgent representations to the Central Government to secure his release by ransom. In August, Father Sands was captured by brigands in Hupeh Province, but, so far, the measures taken by the central authorities to secure his release have proved fruitless, nor have their efforts to trace the murderers of Miss Nettleton and Miss Harrison met with any greater success. The occupation of missionary property in various districts by provincial troops has necessitated on several occasions representations to the local and central authorities.
- 132. Land cases and taxation questions have, as usual, given considerable trouble during the year. In view of the lack of uniformity in the matter of

taxation in different parts of the country, the general practice has been for consular officers, if necessary, to make local representations to the Chinese authorities on behalf of British firms with a view to reaching a settlement, but to leave it in the last resort to the firms themselves to decide how far it is in their interests to resist local taxation demands if pressed. This procedure has, on the whole, worked satisfactorily. The question of the water frontage rights of the Asiatic Petroleum Company and Butterfield and Swire at Shanghai has in particular been the subject of representations to the Central Government, as a result of which the regulations of the Municipality of Greater Shanghai in this connexion have been somewhat modified. Similar difficulties arose as regards foreshore rights, both at Canton and Swatow, and are still the subject of negotiation with the Chinese local authorities.

133. In view of the unsatisfactory treatment of the foreign staff employed by the Chinese Postal Administration and the deterioration of the service, His Majesty's Minister was approached in December by a British employee of the administration with a request that suitable representations should be made to the Chinese Government in the matter. As the service has in the past been regarded as a French preserve, Sir Miles Lampson replied that the initiative lay with the French Legation, who were in full possession of the facts and had promised to communicate with His Majesty's Legation in case intervention were required.

134. At the end of 1930 preliminary agreements were reached between the Ministry of Communications, the Great Northern Telegraph Company, the Eastern Extension Telegraph Company, and the Commercial Pacific Company, respecting the granting of landing licences for submarine telegraph cables and traffic arrangements in connexion therewith. Since that date negotiations have been proceeding for a final agreement, but, in the meantime, the premature action of the local authorities at Foochow and Amoy in taking over the cables of the Eastern Extension Company and the Great Northern Telegraph Company caused considerable disorganisation of traffic. His Majesty's Legation, therefore, drew the attention of the Chinese Government to the unsatisfactory conditions.

135. Although anti-foreign feeling has been evident at intervals during the year, particularly in the case of Japan during the latter part, it has not been directed in particular against British interests. On the other hand, the obstructive attitude adopted by the National Commission for the Preservation of Antiquities towards Sir Aurel Stein and the Haardt Expedition to Sinkiang shows that the anti-foreign feeling still exists under the surface, and is even permitted to intrude into the field of science. In spite of the promise of the Chinese Government not to cancel his travelling pass, Sir Aurel Stein, owing to the consistent obstructions of the local authorities in Sinkiang and the inability of the Chinese Government to give him any assurance that his difficulties would be removed, decided to abandon his expedition, and returned to India in May. His finds were eventually handed over to the local authorities in Kashgar.

The question of the supply of arms to the newly established independent Government at Canton has been a source of some embarrassment to His Majesty's Legation and the Hong Kong authorities. Frequent representations have been made by the Central Government to His Majesty's Minister to detain at Hong Kong consignments of munitions of war destined for Canton. By the terms of the Barcelona Convention the authorities at Hong Kong are precluded from interfering with consignments in transit covered by through bills of lading, whether transhipped at Hong Kong or not, while, on the other hand, they refuse permission for export to Canton of any munitions from store in Hong Kong not covered by the authority of the Nanking Ministry of War. With regard to the export of arms from the United Kingdom, Hong Kong and other colonies, the general attitude of His Majesty's Government has been based strictly on the legal position, namely, that only such consignments are allowed to be exported as are covered by the Central Government permit and the signature of the Chinese Ministry in London. In August His Majesty's Government suggested, with a view to preventing the flood of arms into China, a renewal by British underwriters of their voluntary agreement of 1928, whereby they refrained from insuring or reinsuring any shipments of arms and munitions destined for China. His Majesty's Minister's view was that any reimposition

of the arms embargo was undesirable, and that, as regards the advisability of a renewal of the voluntary agreement, underwriters should be left free to judge all cases on their business merits. As far as consignments of arms to Canton were concerned, both the London and Liverpool Underwriters' Associations agreed in September to refrain from undertaking any insurance.

- 137. On the 9th June His Majesty's submarine "Poseidon" sank, with loss of life, off Weihaiwei, in collision with a Chinese merchant ship. H.M.S. "Petersfield," the Commander-in-chief's yacht, ran ashore in November in a fog north-east of Foochow, and became a total wreck.
- 138. On the 2nd June the Chinese Government officially informed His Majesty's Legation that the limits within which the pursuit of smugglers could be effected would be 12 nautical miles. On instructions from His Majesty's Principal Secretary of State for Foreign Affairs, His Majesty's Legation replied, on the 8th December, that His Majesty's Government were unable to recognise except by bilateral agreement the claim of a coastal State to exercise jurisdiction over foreign shipping outside the 3-mile limit.
- 139. In accordance with the terms of the contract for British naval assistance to China of the 20th June, 1929, Captain Baillie Grohman was appointed head of the British Naval Mission. In March the Chinese Government concurred in the terms of the appointment in an exchange of notes. Not long afterwards the Japanese Embassy in London furnished His Majesty's Government with particulars of a cruiser being constructed by the Japanese Government for the Chinese Government, to be completed in June 1932, the keel having been laid down in February 1931.
- 140. The first anniversary of the rendition of Weihaiwei was celebrated on the 1st October. It may be said that the Chinese administration of the territory has, on the whole, been orderly and efficient, and in the few cases where any representations to local authorities have been required, the results have been uniformly satisfactory. Up to the present no medical officer for the port has yet been appointed under the terms of the Rendition Agreement of the 18th April, 1930.
- 141. Passport regulations requiring foreigners entering Chinese territory to submit for examination passports bearing the visa of a competent Chinese diplomatic or consular authority, were introduced at the beginning of May. The imperfections of the administrative machinery for the operation of the regulations and the lack of uniformity in their interpretation by the various passport offices established for their enforcement, led at once to difficulties and confusion, much of which remain to be cleared up. On the whole, however, it may be said that the Chinese authorities have sought to apply the regulations in a reasonable spirit and in the manner least calculated to give rise to public hardship and inconvenience. There are signs that a definite procedure is gradually being evolved by the process of experience, and it may, therefore, confidently be expected that a satisfactory and uniform system of passport control will ultimately be achieved.
- 142. On the 22nd April the Chinese Government addressed a note to His Majesty's Legation to the effect that as the end of the seventh decennial period of the Treaty of Tientsin of 1858 was reached on the 24th October, 1930, the Chinese Government desired to conclude a new treaty with His Majesty's Government on a basis of equality and reciprocity. The matter was referred to His Majesty's Government for instructions.

(b) Thorburn Case.

143. John Thorburn disappeared from his home at Shanghai on the 31st May under mysterious circumstances. A few days later it was reported that a foreigner answering to Thorburn's description had shot two military police who were patrolling the Shanghai–Nanking Railway line near Quinsan, and that the foreigner had been arrested by the military police. The two police subsequently died of their wounds. As a result of enquiries made by His Majesty's consulgeneral, Shanghai, there were strong grounds for supposing that the foreigner and Thorburn were one and the same person, but the Chinese civil and police authorities all denied any knowledge of the affair. Investigations were there-

fore made at Quinsan and Soochow from the 8th to the 16th June by Mr. Vice-Consul A. L. Scott, and the Ministry for Foreign Affairs were at the same time requested to institute an immediate enquiry. Mr. Scott's investigations went to prove beyond all reasonable doubt that Thorburn had, indeed, been arrested for shooting the military police, and removed to Soochow, where he was kept under detention until the 10th or the 11th June, after which dates all traces of his subsequent movements were lost. In response to further representations for the appointment of a commission of enquiry, Dr Wang stated that the official of the Ministry for Foreign Affairs, who had been sent to investigate the facts, had returned without finding out anything, but that he had now arranged for a fresh enquiry to be conducted by representatives of the Ministry for Foreign Affairs and the Ministry of War. These representatives, who were furnished by His Majesty's Legation with a list of Chinese witnesses and their statements to assist them in their task, left for Soochow at the end of June. A proposal that a British representative should serve on the commission was rejected. On the 16th July Dr. Wang informed Sir Miles Lampson that the commission had reported that no foreigner had been arrested, and that nothing was known of Thorburn's whereabouts. As all possible pressure had been put on Dr. Wang without success, and as it appeared that he was quite incapable of exercising any influence over the military authorities concerned, the matter was referred to His Majesty's Government for instructions. On the 26th July Sir Miles Lampson was instructed to communicate a message to the President of the National Government from His Majesty's Government requesting the Chinese Government to discover the whereabouts of Thorburn, if alive to hand him over for trial, and to inflict suitable punishment on the guilty parties, failing which friendly relations between the United Kingdom and China would be gravely affected. Sir Miles Lampson proceeded immediately to Nanking, impressed upon Dr. Wang the gravity of the situation, and arranged for the transmission of the message to Chiang Kai-shek, who was at the time in Kiangsi. As a result of this action the President at the beginning of August ordered the Vice-Minister of War to make a thorough investigation and probe the matter. According to Dr. Wang this amounted to a fresh investigation, which would be completed in about ten days. Although it appeared that the new investigation was making satisfactory headway, no official report had yet been communicated to His Majesty's Legation, and it was only in September that the Ministry for Foreign Affairs communicated an interim note to the effect that after thorough investigation it had transpired that Thorburn had indeed provoked a calamity and suffered arrest, and that the responsible party was under detention and in process of being tried. Throughout the next few weeks strong and continuous pressure was exercised on the Chinese authorities, including the President himself, to secure full satisfaction. Finally, on the 20th October a formal reply was received from the Chinese Government stating that Thorburn had been shot by the regimental commander at Soochow. The reply contained an expression of regret, an admission that Thorburn should have been handed over to the British authorities, and a statement that the guilty party had been punished and all military commanders notified of the fact. The Chinese reply was accepted by His Majesty's Government as satisfactory.

144. In the middle of November Thorburn's father requested that a claim should be presented to the Chinese Government on his behalf for 100,000 taels, as compensation for expenses and mental anguish sustained on account of the murder of his son. His Majesty's Government considered that a claim for £1,000 was more reasonable, and His Majesty's consul-general, Shanghai, was instructed to explain the position to Thorburn's father. In the meantime His Majesty's Minister broached the subject with the Minister for Foreign Affairs, suggesting that the matter might be settled informally out of court, but by the end of the year no final decision had been taken in regard to the presentation of the claim.

(c) Hankow Assault.

145. On the 6th August a party of British and Americans were returning from the Hankow racecourse in rickshaws through the ex-German concession. In an attempt by the rickshaw-men, being without lights, to elude the police three of the rickshaws collided and overturned, and in the ensuing confusion, which made payment of fares extremely difficult, a hostile crowd collected and

one of the male members of the party was struck. The policeman on duty in the mêlée also attacked and struck him, whilst the women, in their attempt to seek refuge, were indecently assaulted by the crowd. When cross-examined at the police station they were not allowed to communicate with their consular officers. The British and United States consuls-general protested to the Director of the Public Safety Bureau on the following day and requested an enquiry and the punishment of the men concerned. The Director expressed his deep regrets and promised an immediate enquiry and the punishment of the guilty parties. The local authorities at Hankow, however, failed to take adequate steps to deal with the case, and strong representations were accordingly made to the Ministry for Foreign Affairs on the 26th August, drawing their attention to the unsatisfactory and irregular action of the police authorities and suggesting that, in order to effect a prompt settlement of the incident, the police superintendent of the ex-German concession should be removed. The Ministry for Foreign Affairs undertook to investigate the case, and after some weeks His Majesty's Legation's representations bore fruit, for the Ministry for Foreign Affairs informed Mr. Ingram at the beginning of October that the case had been expressed verbally by the chief of the Public Safety Bureau to the British and United States consuls-general, and that the head of the police district had been dismissed. This reply was accepted as satisfactory by the British and United States Legations.

(d) Piracy and Interference of British Shipping.

146. During 1931 only two cases of piracy on the high seas have been reported to His Majesty's Legation, namely, that of the steamship "Hsinming" (China Merchants' Steam Navigation Company) and the steamship "Hanyang" (China Navigation Company (Limited)). The steamship "Hsinming" was bound for Foochow from Shanghai when on the 10th January armed men took control of the vessel. Some of the Chinese passengers and a part of the cargo were taken off north of Bias Bay, but were recovered shortly afterwards owing to the effective action of the Chinese authorities. A second attempt was made on the same vessel later in the month, but the pirates were detected in time in possession of arms and munitions and arrested. The steamship "Hanyang" on her passage from Shanghai to Hong Kong was seized on the 18th November between Foochow and Amoy by a gang of armed pirates from among the passengers. The ship was taken to Namao Island, off Swatow, where a quantity of cargo was removed into a lighter. The facts were reported as soon as possible to the naval authorities at Hong Kong, who sent H.M.S. "Sterling" to Swatow on the 20th November. By arrangement with the Chinese authorities, H.M.S. "Sterling" sailed for Swatow with an armed detachment of Chinese troops on board, and, as a result of combined action, several of the pirates were captured and a part of the cargo recovered.

147. Considerable difficulties have been encountered by British shipping on the Yangtze River owing to the improper searching of vessels for opium, ammunition, &c., by armed Chinese detachments. The steamship "Siuwo" was boarded on the 28th February at Nanking by an armed party in search of contraband, acting on the orders of the garrison commander without the knowledge of the customs authorities. A protest was lodged with the Chinese Government, and it was then agreed that, in cases where the presence of contraband goods was suspected in a British ship, the search warrant should be countersigned by a British consular officer, the customs authorities duly warned and the search carried out by a party in plain clothes. Since the 30th March, when the steamship "Anking" was boarded at Nanking by the customs authorities, accompanied by an armed party, no contravention of the agreement at that port has been reported. Unfortunately, incidents at other ports have been only too numerous. In July and August the steamship "Luenho" and steamship "Kiawo" were irregularly searched at Chungking by armed detachments, and, to prevent a recurrence of such incidents, it was eventually arranged that the British consular and naval authorities should, if possible, be warned of any proposed search and that armed detachments should not go on board.

148. In September the situation became still more unsatisfactory, when the steamship "Tuckwo," steamship "Poyang" and the steamship "Wuchang"

were boarded either at Kowan or Kiangyin by detachments of armed soldiers, acting under instructions from the garrison commander, but without customs co-operation or search warrants. A British gunboat was sent to Kiangyin to prevent further incidents, and the Chinese Government, in response to His Majesty's Legation's strong protest, stated on the 14th October that instructions had been sent to the garrison commander and other military stations to desist from this kind of action. Even so, cases still occurred, so that when it was reported that the steamship "Wusueh" had been searched by an armed party at Nantungchow, H.M.S. "Cricket" proceeded to the spot to investigate. In due course assurances were given by the local Chinese authorities that they would adopt the proper procedure in future. When H.M.S. "Cricket," however, reached Kowan on the 26th December an armed party was caught red-handed searching the steamship "Wuhu." The ringleaders were arrested and later handed over to the Chinese authorities at Chinkiang. His Majesty's Legation again drew the serious attention of the Chinese Government to their complete failure to implement their promises, and the latter, in expressing their regret, undertook fullest investigation, punishment of the guilty parties and the despatch of fresh stringent instructions to all concerned.

(e) Kuomintang in Malaya.

Towards the end of 1930 the whole question of the suppression of the Malayan branches of the Kuomintang and the particular cases of the two Chinese Chen Lo-sheng and Fang Chih-chen, who had been banished from Malaya by the British authorities, was taken up vigorously by the Minister for Foreign Affairs with His Majesty's Minister, and at the end of the year Sir Miles Lampson left for Singapore to discuss the problem with the British authorities on the spot. At the discussions, which opened on the 8th February, Sir Miles Lampson pointed out that the crux of the matter was whether or not the Tang should be allowed to establish Tangpu in Malaya. He realised the danger of organised Kuomintang there, but took exception to the existence of legislation under which the Tang was ipso facto a proscribed illegal society. He urged that the legislation in force should be amended so as to remove the stigma of illegality on the ground that the Chinese Government, with whom His Majesty's Government were on friendly relations, was an off-shoot of the Kuomintang, and the position was therefore embarrassing and illogical, if the Kuomintang were banned under legal legislation in Malaya. The representatives of the Malayan Governments held the view that a real danger existed if the Tang were allowed to organise and establish central and branch offices in Malaya, that the Tang was not, in fact, illegal in Malaya provided that it did not apply for registration, and, further, that it was impossible to amend the local ordinances. After exhaustive discussions, it was finally decided (a) that His Majesty's Minister, after drawing the attention of the Chinese Government to the complaints of the British authorities against the improper activities of the Kuomintang, should endeavour to obtain an assurance from them that they did not countenance any improper interference in domestic affairs in Malaya or the establishment of central and branch Tangpu in that territory; and (b) that the Malayan Governments for their part would, on the receipt of such an assurance, amend the present legislation in such a way that a society, though unregistered, and therefore unlawful, if not actually organised in the colony, would not be regarded as a society within the meaning of the Societies' Ordinance, and would not therefore be illegal. As regards the cases of the two Chinese, it was agreed that their sentences should be alleviated on condition of their proper behaviour. This concession was made with a view to reaching a settlement on the major issue. Other questions discussed related to the interference from China with educational and other domestic affairs and the functions of Chinese consuls.

150. On his return to Nanking in March, His Majesty's Minister communicated to the Minister for Foreign Affairs a draft exchange of letters on the lines of the Singapore proposals. Dr. Wang was willing to give assurances as regards the proper behaviour of the Kuomintang, but was unable to accept the proposal that there should be no organisation in Malaya, and on the 12th March handed to Sir Miles Lampson a counter-draft proposing that the holding of meetings by members of the Tang should be legal, and that "correspondence offices" instead of branch offices should be established. This

draft was considered unacceptable. Finally, agreement was reached on the 1st April in the form of an exchange of letters whereby Dr. Wang gave the necessary assurances against improper activities by the Kuomintang, and added that party offices would not be established in Malaya. Sir Miles Lampson accepted these assurances, and stated that in view thereof the Malayan authorities would amend their legislation on the lines recommended by the Singapore Conference. As regards the cases of Chen and Fang, Dr. Wang stated that he had received promises of their proper behaviour in future, and Sir Miles Lampson undertook to communicate this assurance to the British authorities for favourable consideration. The agreement was subsequently approved by His Majesty's Government.

- 151. The banishment order against Chen was cancelled on the 11th May, but no final decision yet appears to have been taken in the other case. The necessary amending legislation was passed on the 31st August. In the meantime documentary evidence came into the hands of the Singapore authorities, showing that the agreement was being violated on the Chinese side by the opening in Malaya of Kuomintang party branches. The facts were communicated to Dr. Wang, who in justification could only reply that the action of the Kuomintang had evidently been taken in ignorance of the terms of the settlement. Although additional evidence was communicated to His Majesty's Legation later by the Malayan authorities, it was considered inadvisable to take any further action with the Chinese Government for the time being.
- 152. Difficulties arose in September over the visit of Chow Chi Kang, vice-chairman of the Commission for Chinese Affairs, to Singapore for the investigation of conditions of overseas Chinese. The Malayan authorities refused to allow him to carry out his task in view of the scope of his mission, and on the ground that proper notification of his visit had not been made. The attention of the Chinese Minister for Foreign Affairs was immediately drawn to the irregularity of this action, and Chow Chi Kang, whose activities throughout had been far from satisfactory, was compelled to leave Singapore without fulfilling his mission. He was followed shortly afterwards by Ting Chao-wu, second Special Commissioner, who similarly was not permitted to land at Singapore. Although at the time the Chinese Government were highly incensed at our action, nothing further was heard of the incidents.

(3) Canada.

- 153. The Honourable Herbert Marler, His Majesty's Minister for Canada in Japan, visited Nanking in January to discuss with the Chinese Government the possibility of the sale of Canadian wheat. After protracted negotiations both with the Chinese authorities and private interests, it was not found possible to reach any satisfactory agreement. Later in the year the Department of Trade and Commerce at Ottawa decided to open two new offices of the Canadian Commercial Intelligence Service in Tientsin and Dairen.
- 154. On instructions from His Majesty's Government in Canada, His Majesty's Legation informed the Chinese Government on the 24th December that the regulations imposing a fee of 10 gold dollars for the endorsement by Canadian immigration officers of passports of persons of Chinese origin proceeding to Canada had been cancelled, and that no fee was now payable for such visas.
- 155. As a result of the activities of the anti-Japanese Boycott Association at Shanghai in December, a consignment of Canadian dry salt herrings destined for the interior was seized. Representations were immediately made to the Chinese Government with a view to instructions being issued for the prevention of any further obstruction of this nature.
- 156. At the end of the year His Majesty's Legation furnished His Majesty's Government in Canada with a list of Canadian nationals resident in China on the 1st June, 1931.

(4) Japan.

157. The most fateful event of the year in China has been the Japanese attack on Manchuria.

158. During the beginning of the year Japan's policy towards China appeared to be still conciliatory. She seems, however, to have felt a growing uneasiness at the continued refusal of the Chinese authorities to recognise her special rights in Manchuria, conferred by the treaty of 1915, and at the growing competition of the Chinese Railways with the South Manchuria Railway. Early in the year it was stated that a Sino-Japanese conference was to be held in Mukden to discuss railway matters and other outstanding questions in Manchuria. The conference, however, came to nothing owing to the evasive attitude of the Chinese authorities. Japan was also disturbed at the intervention of Marshal Chang Hsueh-liang in the politics of China proper, and at the close relations established between him and Marshal Chiang Kai-shek, which seemed likely to lead to the assimilation of Manchuria to the rest of China. She saw in this prospect a threat to her position in Manchuria.

159. In July trouble broke out between Chinese peasants and Korean farmers at Wanpaoshan in Kirin. This was followed by an anti-Chinese outbreak in Korea, in the course of which some thousands of Chinese are said to have been massacred by Koreans. As a result of this a boycott of Japanese goods was started in Shanghai, but it never assumed serious proportions. In the last days of June a Captain Nakamura, a Japanese intelligence officer, was murdered by Chinese soldiers on the Mongolian frontier. This greatly inflamed the Japanese army and appears to have precipitated the crisis.

160. On the night of the 18th September when the Nakamura case seemed on the point of being settled, the Japanese forces in Mukden carried out a coup de main, drove out the Chinese from the main points of military importance and took control of the city. The Chinese troops in Mukden, who had orders not to resist any aggressive measures, fled. The pretext given by the Japanese was an alleged attack on the South Manchuria Railway line.

161. On the same night and the following day Changchun, Newchwang, Antung and other places on the South Manchuria Railway were occupied in a similar manner by the Japanese forces stationed on the Railway Zone. Since then they have extended their virtual occupation to the larger part of Manchuria, setting up nominally independent Chinese Administrations at various places under the protection of the Japanese forces. At the time of the clash Marshal Chang Hsueh-liang was residing in Peking, whither he had transferred his headquarters in July. Most of the Provincial Government fled from Mukden, and a shadow Government was set up at Chinchow on the Peking-Mukden Railway under the orders of Marshal Chang. Affairs in Mukden were nominally in the hands of a Chinese committee of public safety acting with Japanese advisers, until the 10th November, when a new Provincial Government was set up under Japanese auspices.

162. In Kirin General Hsi Chia, the acting head of the Provincial Government, was compelled by the Japanese to establish a new Provisional Government under their supervision. Heilungchiang, lying outside the Japanese sphere of influence, remained under the control of authorities owing allegiance to the Central Government until the 18th November, when Tsitsihar, the seat of General Ma Chan-shan's Provincial Government, was occupied by Japanese troops after an attack carried out at their instigation by their Chinese satellite, Chang Hai-peng, had failed. Except in the Tsitsihar campaign the Chinese troops in Manchuria offered no serious opposition to the Japanese encroachments. The Chinese Government conscious of their helplessness made no attempt at military resistance and adopted no measures of reprisal, but appealed to the League of Nations under article 10 of the Covenant, and trusted to the Powers represented on the Council and to the United States Government to save Manchuria for them. The Japanese Government on the other hand, showed themselves determined to resist any attempt at interference in the Manchurian question either by the League or by individual Powers, and declared that the crisis could only be settled by direct negotiations between the parties.

163. A special meeting of the Council of the League met on the 2nd September, but all that could be achieved was the adoption on the 30th September of an unanimous resolution taking note of the assurances by Japan that she had no territorial designs on Manchuria, and that the Japanese

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troops would be withdrawn (to the South Manchuria Railway Zone) as soon as the safety of life and property of their nationals was assured, and by China that she would be responsible for affording protection to Japanese life and property as the Japanese troops were withdrawn. Both sides were urged to do all in their power to restore normal relations, and a further meeting of the Council was set for the 14th October.

- 164. The Japanese continued to maintain with some show of reason that the disturbed condition of the country contained dangers to their nationals and to make this a justification for not withdrawing their troops, while the anti-Japanese boycott was revived in China proper, especially at Shanghai. On the 11th October the Japanese Minister presented a memorandum at Nanking demanding the cessation of the boycott which, it was alleged, was being fostered by the Chinese Government and constituted a hostile act.
- 165. On the 8th October Japanese aeroplanes dropped bombs on Chinchow, with the object apparently of dislodging the remnants of the Liaoning Provincial Government.
- The Council of the League reassembled on the 13th October, but failed to bring about any measure of agreement, owing to the refusal of the Japanese Government to accept any fixed date for the withdrawal of their troops or to agree to open negotiations with the Chinese with any kind of neutral participation. A representative of the United States Government attended the meetings of the Council by special invitation, an objection by the Japanese Government being overruled. A resolution was finally recorded on the 24th October with the assent of all except the Japanese member, calling upon Japan to complete the evacuation of her troops from the points they had occupied before the next meeting of the Council, recommending the appointment of representatives of both sides to make the necessary arrangements for the transfer of control, and the association with them of neutral observers and calling upon the parties to begin negotiations upon all outstanding questions as soon as the evacuation was completed. The Council then adjourned till the 16th November. Two days later the Japanese Government issued a statement of their position with regard to direct negotiations, laying down five fundamental points, the acceptance of which must precede the opening of negotiations with the Chinese Government. These points covered the suppression of the boycott and respect by China of Japan's treaty rights in Manchuria (i.e., recognition of the treaties of 1915 and 1917, of which China refuses to acknowledge the validity). During the course of the Council meeting a number of the signatories of the Kellogg Pact made concerted representations to both parties calling their attention to their obligations under article 2 of the pact. Both sides in reply declared their intention to respect these obligations.
- 167. When the Council met again the Japanese attack on Tsitsihar had begun. There were also local disturbances at Tientsin leading to firing in the neighbourhood of the Japanese Concession, which, however, eventually died down after the Chinese had agreed to withdraw their troops 20 li from Tientsin under an old arrangement concluded in 1902. At the same time the Japanese threatened to move against Chinchow where they alleged that the troops of Chang Hsuehliang were massing to attack them. In order to keep watch on events and furnish reliable information, observers from the British, French, Italian and United States Legations were despatched to Chinchow, where they remained till the end of the year. They reported no offensive preparation of any kind by the Chinese. An attempt was made by the Council to arrange for the establishment of a neutral zone between the Japanese and Chinese forces at this point, but failed owing to the outcry aroused in China by the suggestion that the last foothold in Manchuria should be abandoned. This outcry was eventually largely responsible for bringing about the fall of the Government in December.
- 168. No progress was made by the Council towards a solution of the dispute, and it was finally agreed that the League should despatch a commission to China to enquire into the situation. The Japanese insisted that this commission should have no title to recommend troop movements or to intervene in any discussions between the parties. It was declared, however, that if the commission found that the parties had not carried out their undertakings recorded in the League resolution of the 30th Sepetmber, it should immediately report to the Council.

169. During the above discussions the threatened attack on Chinchow was postponed. It became clear, however, that the Japanese were determined to remove this remaining outpost of Chang Hsueh-liang's authority in Manchuria. Finally, on the 28th December under the threat of a Japanese advance, the Chinese evacuated Chinchow and retired inside the Great Wall; the Japanese troops occupied the town and the Peking-Mukden Railway up to Shanhaikuan on the first days of 1932. By the end of the year they held all the strategic points in Manchuria except Harbin, which they had refrained from occupying possibly out of respect for the Russian interests on the Chinese Eastern Railway which were centred there. The Civil Administrator of Harbin, Chang Ching-hui, was, however, on friendly relations with them, and discussions were on foot with a view to establishing him as head of the Heilungchiang Provincial Government under their auspices, in place of General Ma Chan-shan.

(5) Russia.

(a) Chinese Eastern Railway.

- 170. The decline in the value of silver caused the freight charges of the Chinese Eastern Railway, which are calculated on a gold rouble basis, to rise to exorbitant figures in terms of local currency. The railway was thus placed in a disadvantageous position and suffered a severe diminution in traffic due to the fact that a large proportion of goods imported into Harbin and Heilungkiang which it would normally have handled were diverted to other lines.
- 171. Mo Teh-hui returned to Moscow in the spring and early summer the Sino-Soviet deliberations resumed their weary course. At the end of the year little progress appeared to have been made, although the path towards a resumption of Sino-Soviet relations is reported to have been cleared by the Soviet Government tacitly agreeing to drop the question of the Habarovsk Protocol.
- 172. It appears that in the course of its discussions the conference touched somewhat academically upon the question of the redemption by China of the Russian share in the Chinese Eastern Railway, and in June it was even rumoured that an agreement had been reached whereby China would assume full control of the railway, granting to Soviet Russia in return the right for a period of eight years to import Soviet goods into China duty free. The remitted duty on these goods would be regarded as having been paid by China to Russia as the purchase price of the Russian share of the line. This report was, however, categorically denied by the Chinese Government.
- 173. Since the outbreak of the Sino-Japanese dispute there have been frequent rumours that the Russian interest in the line or at any rate in the Changchun-Harbin section of it, was to be purchased by Japan, but these reports have been denied.

(b) Sino-Soviet Relations.

- 174. As reported above, little tangible progress was made during the year towards a resumption of Sino-Soviet relations. Since the present Sino-Japanese dispute began, however, there has been a certain amount of irresponsible talk, even in Chinese Government circles, of obtaining Russian assistance with which to drive Japan from Manchuria. There seems, however, little reason to believe that Russia, preoccupied as she is with her own internal problems, is disposed to intervene in a struggle which does not directly concern her, and from which she is unlikely to derive any great benefit.
- 175. Comintern propaganda in China and the assistance given by Russia to the Chinese Communist party is dealt with in another section.

(6) United States.

176. Close and friendly relations have been maintained between His Majesty's Legation and the United States Legation, and there has at all times been a frank interchange of information on internal and foreign questions. This

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state of affairs has been particularly noticeable in the extra-territoriality negotiations; in this connexion Mr. Johnson was instructed by the United States Government to afford Sir Miles Lampson all moral support in his task. In return for their loyal co-operation the United States Legation were kept fully informed of the course of negotiations at all stages.

177. Apart from the wheat loan negotiations with the Chinese Government at the time of the Yangtze River floods, the Hankow assault incident in which United States citizens were involved, and the constant efforts made by the United States Legation in co-operation with the representatives of other Powers to find a solution of the Sino-Japanese crisis in Manchuria, all of which questions are referred to elsewhere in this report, there is little to record in the matter of Sino-American relations, which have on the whole remained cordial throughout the year. The case of Dr. Tucker, however, a member of the American Board Mission at Tehchow, threatened for a time to assume some importance. In July he shot a Chinese whom he caught red-handed rifling his safe, and was thereupon imprisoned by the Chinese authorities. It was only after strong representations that he was released and handed over to the United States authorities. At various times of the year cases have occurred of American missionaries being captured and held to ransom by bandits.

178. Dr. Yen Hui Ch'eng was appointed Chinese Minister to Washington to succeed Dr. C. C. Wu on the latter's resignation, and in December proceeded to Geneva as Chinese representative on the League of Nations.

(7) France.

In March M. Haardt, one of the directors of the Citroen Motor Company, headed the western section of an expedition with motor caterpillars from Beirut to Peking via Iraq, Persia and India for the purpose of scientific investigations. A little later, in spite of numerous difficulties and restrictions, an eastern section, including Chinese representatives in an advisory capacity, started out from Peking to meet the expedition in Sinkiang. Unfortunately disagreement arose between the French and Chinese members of the eastern section near Ninghsia, where Lieutenant Point, one of the French members, is said to have assaulted a Chinese scientist attached to the expedition. The latter returned to Peking and opened a bitter press campaign, accusing the French of violating their agreement. At the same time the National Association for the Preservation of Antiquities requested the Chinese Government to take all possible measures to restrict the activities of the expedition, and even urged the provincial authorities in Sinkiang to detain it. In consequence endless difficulties were encountered, and the eastern section only reached Urumchi on the 8th July. Later it proceeded to Kashgar where it was eventually joined by the western section from India. At the end of the year the two sections had not yet reached Peking.

180. Owing to the publicity given in press articles in April to the possibility of a French occupation of the Paracel Islands, enquiries were made by His Majesty's consular officers at Shanghai and Canton as to the intentions of the Chinese authorities regarding the maintenance of their sovereignty over these islands, and it was ascertained that the customs authorities and Cantonese Government were discussing plans for the lighting of the territory. In July His Majesty's Embassy in Paris approached the French Government in the matter regarding their intentions, and the latter replied that the question of the title to sovereignty over the islands was still under examination by their legal advisers.

181. The Shanghai French Mixed Court Rendition Agreement was signed on the 25th July, and came into force on the 1st August. It follows the general lines of the agreement for the handing over to China of the Provisional Court in the International Settlement, except that it provides for the appointment of an adviser, on the recommendation of the French Government, to deal with the administration of the prisons of the concession.

182. In December reports appeared in the press of the alleged massing of French troops on the Tongkin-Kwangsi frontier. These reports were denied in French official circles. Rumours of a secret treaty between France and Japan,

whereby in consideration for French military support in Manchuria the Japanese Government would give France a free hand in Kwangsi Province, were similarly denied.

183. In March the French Minister communicated to the Chinese Government the proposals of his Government on the subject of extra-territoriality, but he does not appear to have made much progress in his negotiations. At the end of April His Majesty's Minister handed to M. Wilden the text of the articles of the proposed extra-territoriality treaty with China, on which agreement has so far been reached.

(8) Germany.

- 184. There is little to record in the matter of Sino-German relations during 1931, which were mainly confined to aviation development and the activities of the German Military Mission. This mission employed by Chiang Kai-shek is reported to consist of about fifty advisers and instructors distributed at Nanking, Hangchow, Peking, Shanghai, Pengpu and Hankow on a two years' contract. In September the Cantonese Government threatened to boycott Germany on the ground that these experts were manufacturing poison gas. Although the whole question of gas warfare had undoubtedly been studied by the Chinese military authorities in consultation with their German advisers, and experiments may even have been carried out, there is nothing to show that gas has been manufactured, or much less employed in any quantities.
- 185. In the field of aviation German firms have made considerable progress in the promotion of their commercial interests by the sale of machines to the Chinese authorities (see section on Aviation).
- 186. General Liu Wen-tao was appointed Chinese Minister to Germany and Austria on the 17th October and reached Berlin on the 30th December.

(9) Belgium.

187. The Sino-Belgian agreement for the rendition of the Belgian concession at Tientsin was signed on the 31st August, 1929, but the exchange of ratifications and the formal ceremony of rendition only took place on the 15th January, 1931, in the presence of the Chinese Minister for Foreign Affairs and the Mayor of Tientsin. The Belgian Minister, who had intended to be present at the ceremony, was taken seriously ill on his arrival at Tientsin. The concession is completely undeveloped, as it was thirty years ago, except for the International Export Company's factory, and its rendition, therefore, cannot have given the Chinese Government any real satisfaction, particularly in view of the fact that one of the conditions of the agreement was the reimbursement by the Chinese Government to the Belgian Government of the outstanding debts incurred by the municipality of the concession, amounting to 93,000 Tientsin taels. The Chinese Government only carried out this condition after much hesitation.

(10) Portugal.

188. In August the Portuguese Minister informed His Majesty's Minister that the Chinese Minister to Lisbon had been withdrawn and that the Chinese Legation would henceforward be under the orders of the Chinese Chargé d'Affaires in Madrid. Although he had already informed the Chinese Minister for Foreign Affairs of the unfortunate impression this arrangement had made on the Portuguese Government, he would be grateful if His Majesty's Minister could ascertain privately from the Chinese Government the reason for this step. In response to unofficial enquiries, C. T. Wang informed Sir Miles Lampson that there had been some misunderstanding, seeing that the present arrangement was purely a provisional one pending the appointment of a new Minister to Lisbon.

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(11) Treaties with Secondary Powers.

- 189. Ratifications of the Sino-Polish Treaty of Friendship, Commerce and Navigation signed on the 18th September, 1929, with the additional protocol signed on the 1st July, 1930, were exchanged by the Chinese Minister for Foreign Affairs and the Polish delegate in Shanghai on the 17th July. The treaty was brought into force on the 9th July and M. de Weydenthal was nominated first Polish Minister to China. Mr. Wang Kwang-ch'i was appointed Chinese Minister to Poland as from the 13th August. By an exchange of notes later it was agreed to make the Free City of Danzig a party to the treaty.
- 190. On the conclusion of the negotiations for a Sino-Turkish treaty, the Turkish Legation in China was, for reasons of economy, closed down provisionally in July. It is reported that the treaty will be signed in Berlin or Geneva.
- 191. A treaty between the Netherlands and China for readjusting matters relating to jurisdiction over Netherlands subjects in China was concluded by the Netherlands Minister and the Chinese Minister for Foreign Affairs at Nanking on the 23rd April, and notes were exchanged on the same date.
- 192. On the 23rd April an exchange of notes took place between the Norwegian Minister in China and the Chinese Minister for Foreign Affairs to the effect that Norwegian nationals in China should come under Chinese jurisdiction simultaneously with the nationals of those countries which directly participated in the discussions at the Washington Conference. These stipulations only affected those provisions of the Sino-Norwegian Treaty of 1847 relating to matters of laws and jurisdiction.

(12) League of Nations.*

- As stated in the Finance Section of this report, China has more and more been availing herself of the advice of the technical branches of the League of Nations for the improvement of her administrative services. In January the Chinese Government expressed their appreciation to the League on the arrival in China of Dr. Rajchman, Director of the League Health Organisation. At their request, Sir A. Salter, Director of the League Economic and Financial Organisation, and M. R. Haas, Director of the League Transit and Communications Organisation, reached China in March, the former to examine questions relating to the effect of China's economic activities on the world depression, and the latter to discuss the problems of inland waterways and land reclamation. The Central Government took the opportunity of discussing with them proposals for closer co-operation with the League, and in a further communication to the latter in April expressed the hope that their technical organisations would be continuously available to advise the Chinese Government and the newly-created National Economic Council with its plans of reconstruction. In addition to the foregoing, four League educational experts visited China in September and October to inspect educational institutions, and Sir John Simpson, with a League Medical Mission, came out in October to assist with flood relief. The question of factory legislation in Shanghai was similarly investigated by League experts in October, and at the end of the year representatives from Geneva were expected to arrive in China to advise principally on the river system of North China. Although it may be observed China is anxious for League advice, it remains to be seen how far any recommendations which may be made will really be put into practice.
- 194. In September the Chinese Government requested His Majesty's Government in the United Kingdom to give China their full support for their candidature as member of the League Council. China was shortly afterwards elected unanimously as a non-permanent member of the Council.
- For the appeal of the Chinese Government to the League of Nations in connexion with the Sino-Japanese dispute in Manchuria, see paragraphs 162-168 above.

(13) International Settlement at Shanghai.

(a) Greyhound Racing.

The Shanghai Municipal Council decided that the operation of the dog-racing tracks in the settlement would not be permitted after the 31st March, 1931. His Majesty's consul-general was instructed to inform the chairman of the council that while the responsibility for dealing with this matter rested primarily with the council, the latter's action in closing these establishments appeared to the British authorities to be in the best interests of the settlement. An attempt to hold a race meeting at the Luna Park track on the 4th April Feeling that action was prevented by the police without any trouble ensuing. against the council in the court of consuls would have no chance of success, the interests concerned took legal action against the chairman of the council and the commissioner of police, who both happen to be British subjects, individually in His Majesty's Supreme Court. The action was summarily dismissed by His Majesty's judge on the ground that no reasonable cause of action had been shown. Appeal was lodged with the full court against this judgment, and was allowed. The case will, therefore, have to come to trial in the ordinary way, and the hearing will probably take place in February or March 1932.

(b) Extra-Settlement Roads.

196. In the early months of 1931 the Chinese continued to pursue a policy of steady encroachment on the council's control over these roads, and the council asked if they could rely on the support of His Majesty's Government in forcible resistance to these measures. His Majesty's Minister was instructed to inform the chairman of the council in reply that, while His Majesty's Government were prepared to support the council in their rights, under land regulation No. 6, to maintain the roads, pending a settlement by negotiation and compromise, it should be made clear that the question primarily concerned all the Powers interested, and that the council must assume responsibility for any action taken to assert their rights and that it was highly improbable that His Majesty's Government would use force for the maintenance of a contested privilege of this nature. The council were opposed to a compromise by which they should be allowed to repair the roads, while abandoning the right to police them, and to collect municipal rates from foreign property abutting thereon. The Officer Commanding the British Forces in the Shanghai Area also pointed out that, as these forces were situated outside the settlement, the position from a defence point of view would be untenable if complete Chinese control of the outside roads were recognised. Sir Miles Lampson was reluctant to raise the question formally with the Minister for Foreign Affairs as a separate issue in advance of the conclusion of the extraterritoriality negotiations. Finally, a temporary compromise was reached locally, whereby the settlement authorities were allowed to repair the roads, provided they gave notice to the Chinese and refrained from any new constructive work. Negotiations for a settlement of the question were initiated in May between the Chinese Mayor of Greater Shanghai and the Shanghai Municipal Council, but Meanwhile, one or two unfortunate collisions between the led to no result. Chinese and the settlement police on property adjoining the outside roads, during the summer, fortunately had no very serious consequences.

(c) Judge Feetham's Report.

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197. This report was published in three volumes during the early summer of 1931. The first volume dealt with the facts of Shanghai's history and problems from the foreign point of view, and emphasised the benefits derived from a "rule of law" based on Anglo-Saxon models. The second volume dealt with the existing Chinese administrative system generally, and expressed views as to the future status and constitution of the International Settlement. Judge Feetham took the line that rendition could not be contemplated till the idea of the "rule of law" had taken root in China and was embodied in an effective form in the institutions of the country, which was a question not of years, but of decades. The third volume of the report dealt exclusively with the question of the external roads built by the Shanghai Municipal Council. The Chinese press comment on the report was curiously scanty and on the whole restrained; the proposals

contained in the report for the future government of Shanghai were generally regarded as hardly practicable, and to take no account of Chinese national aspirations.

(d) Fourth Biennial Conference of the Institute of Pacific Relations.

198. This conference was held at Shanghai from the 24th October to the 3rd November, 1931. The institution was on this occasion invited by the Chinese to hold its gathering in China, and the site selected was Hangchow. But as the Chinese authorities could not at that moment guarantee the safety of the delegates at Hangchow, it was eventually decided to hold the conference in the International Settlement at Shanghai.

III.—RAILWAYS.

(a) General.

198A. In spite of comparative freedom from civil strife, the Chinese railway system showed no marked signs of progress or financial rehabilitation during the past year, and at the close of the year the Sino-Japanese situation threatened to affect the best-managed of the railways so seriously as to put the clock back several years as far as reconstruction and reorganisation are concerned. On the Peking–Mukden (now called Peiping–Liaoning) and the Shanghai–Nanking Railways, the potential damage to the interests of British bondholders is considerable, while the Tientsin–Pukow line, which connects with both, inevitably suffers from the misfortunes of its fellows. Considerable assistance is, however, likely to be forth-coming, in the shape of materials and rolling-stock, from the British indemnity funds. The Peking–Mukden, Tientsin–Pukow and Shanghai–Nanking lines were considerably interfered with, and their traffic interrupted in November and December by large bodies of students clamouring to be taken to the capital to protest against the weak policy of the Government in face of Japanese aggression.

(b) Loan Situation.

The loan situation (see also under Finance) shows no sign of improvement. No payments have been made on the Canton-Kowloon Railway Loan of 1907, or the Tientsin-Pukow Railway Loans of 1908 and 1910. Arrears on the Hukuang Railways Loan of 1911 now amount to £2,002,675 7s. 6d. of the Canton-Kowloon Railway Loan to £962,136 16s. 4d., of the Tientsin-Pukow Railway Main Loan of 1908 (British portion) to £905,288 10s. 9d., and of the Supplementary Loan of 1910 (British portion) to £678,792 15s. The representatives of the British, French and American group banks interested in the service of the Hukuang Railways Loan have asked their respective Legations to urge the Chinese Government to give effect to article 9 of the Loan Agreement, which provides that, in the event of the abolition of the li-kin required to provide the service of the loan, an equivalent charge will be laid upon the increased customs revenues. Similar representations were recently (in November 1931) made by this Legation to the Chinese Government in respect of the identical article 9 of the Tientsin-Pukow Loan Agreement of 1908, but no reply has yet been received, the interests of the Ministry of Finance and of the Ministry of Railways being in this matter opposed to one another, each being anxious to saddle the other with the responsibility for payment of the loan services. The Chinese Government again failed to pay the (third) instalment of principal due on the Shanghai–Nanking Railway Loan of 1903 in June 1931, making total default in respect of the two instalments, due in June 1930 and 1931, £232,508. The Railway Administration also failed to pay at due date (January 1931) the first two instalments payable in respect of the rolling-stock purchased for the railway by the British and Chinese Corporation, to an amount of £156,000, under an agreement dated the 21st June, 1929. The Ministry of Railways later stated its intention of paying for this material out of British indemnity funds. Hangchow-Ningpo Railway Administration also failed to pay the half-yearly amortisation amounting to £37,500, due for payment in London on the 1st December, 1931. This, coupled with the similar amount of amortisation due The Shanghaifor payment on the 1st June, 1931, and unpaid, amounted to a total default of £75,000. The existing high exchange rate for gold was made the principal excuse for these various defaults.

(c) New Construction.

200. Once again there is little new construction to be recorded on the railways in China proper, though the southern section of the Canton-Hankow Railway, northwards from Canton, continues to make some progress. It is expected that work on the Shiuchow-Lokchang section of this railway will be completed in the summer of 1932. It is said that £170,000 will be supplied for the purpose from the British indemnity funds. The next sector northwards from Lokchang to Pingshih (35 miles) is now being surveyed, but presents considerable engineering difficulties. It is also said that a sum of £200,000 a year is to be allotted from the British indemnity funds for this new constructional work and for the completion of the whole line over a period of fifteen years. It is hoped, however, to finance the construction out of these releases in such a way that the work may be completed within four years.

(d) Canton-Kowloon Railway.

201. Early in 1931 the Ministry of Railways began pressing for the revision of the Canton-Kowloon Railway Working Agreement of 1911, which governs the operation of the two sections, British and Chinese, of the line (see paragraph 288 of last year's report). Delegates were despatched to Canton and Hong Kong with this object in view. On the plea that the Hong Kong Government were unwilling to negotiate the desired revision, the Ministry of Railways gave notice of termination of the agreement under article 41. The attitude of the Hong Kong Government was, in brief, that no concessions would be made in regard to the proposed revision until the Chinese Government had taken steps to bring the efficiency of their section of the line within measurable distance of that of the British section. The notice of termination of the working agreement was to become effective on the 24th March, 1932. A reply was returned to the Minister for Foreign Affairs proposing that the Ministry of Railways should, in the first instance, formulate their suggestions for revision in writing, as a preliminary to negotiations between the Chinese Government and the Government of Hong Kong for the final settlement of a new agreement, so as to give ample time for revision before the notice of termination of the existing agreement became effective. This note was sent in on the 19th May, 1931. No reply has been received, though the Chinese director of the railway is reported to have declared to press representatives in Canton in November last that the Provincial Government, which had by then taken over control of the railway, did not intend to press for revision of the agreement for the time being.

(e) Peking-Mukden (Liaoning) Railway.

202. As a result of the Japanese action in Manchuria (described elsewhere in this report), the whole section of the line outside the Wall between Mukden and Shanhaikuan had, by the end of the year, fallen under Japanese military control, and the Chinese Railway Administration at Tientsin were unable to run any trains over it, through communication being entirely interrupted. Many trains (partly composed of South Manchuria Railway coaches) were being run on the section outside the Wall, though there was considerable damage to the railway instruments, as well as to the track and bridges in places west of Chin-hsien. A new railway administration had been formed at Mukden for the Mukden-Shanhaikuan (Feng-Shan) section. The railway was thus again divided into two sections, as it had been in the course of China's civil wars of 1922, 1924 and 1928. The manner of this division raised in an acute form the rights of the British bondholders under the original loan of 1898, and of other British creditors having a lien on the railway's earnings. The representatives of the British and Chinese Corporation succeeded, however, in persuading the Japanese advisers to the new régime at Mukden to make payments, out of monies standing to the credit of the Chinese Railway Administration in Chinese banks in Mukden, of £50,000 on account of five months' (September to January) Double Track Loan (of 1921) instalments, and £15,000 odd on account of two months' (December and January) instalments of the 1898 loan service. At the moment of writing the railway administration at Tientsin are endeavouring to arrange the resumption of through traffic between Peking and Mukden. The attitude of His Majesty's Minister in this matter is that the Legation cannot be drawn in as

between Chinese and Japanese, and that his concern is confined to the protection, to whatever extent lies in his power, of the British financial interests involved.

(f) Hulutao Harbour.

203. The work on the Hulutao harbour contract continued throughout the year, in spite of constant difficulties between the contractors, the Netherlands Company and the Chinese Harbour Bureau. All operations ceased, however, when the Japanese military occupied the port at the end of the year, and the contractors will have considerable trouble to secure either from the old or the new provincial régime the payments due to them.

(g) National Railway Conference.

204. A National Railway Transport Conference was held in March 1931, at which many admirable, though stereotyped, resolutions were passed for the improvement of the railways, which more recent events will render even more difficult of execution than they were then. Reduction of freight charges on native goods was urged among other "reforms." In spite of the assurances of the Minister of Railways (see paragraph 274 of last year's report) in regard to the abolition of discriminatory freight charges on the Chinese Government railways, foreign firms, especially the cigarette manufacturers, continued to complain of such discrimination, which involved very large excess freight charges, throughout the past year, and renewed representations had to be made on more than one occasion to the National Government on the subject of this practice.

(h) Debts to British Ex-employees.

205. The question of the sums still owing to their British ex-employees by various Railway Administrations was still unsettled at the end of the year, though every endeavour is being made to settle the accounts with the Ministry of Railways and to obtain satisfaction for the individuals concerned.

206. The Manchurian railways are dealt with in this report under the heading of Manchuria.

IV.—FINANCE.

(a) General Situation.

207. Any prospects of improvement in the financial situation in China, which may have been apparent in the earlier months of 1931, disappeared with the various national disasters—for they were nothing less—which took place in the latter part of the year. The unfortunate split between Nanking and Canton was followed by the widespread floods in the Yangtze Valley, involving enormous destruction of life and property, and, finally, the Manchurian crisis, coming at a time of world-wide trade depression, threatened to plunge China once and for all into the financial abyss which has threatened to engulf her many times since the inauguration of the republic. Vague, and largely unfounded, rumours of the Government's calling a moratorium on foreign loans were followed at the end of the year by actual threats of a moratorium on domestic loan issues. These threats, which were put out by the new Government under Mr. Sun Fo and which have not as yet been carried out in practice, were made mainly with a view to blackmailing the Shanghai Chinese bankers, who have always loyally supported the National Government by taking up large quantities of these domestic issues and are now suffering severely from the heavy depreciation in their value, into providing the new Government with funds of which it stood in dire need, for carrying on the administration. The net result has been that the Government have now secured a promise of immediate assistance to the extent of 8 million dollars for one month to tide over the crisis, while the Inspector-General of Customs has been authorised to issue a statement to the effect that there will be no moratorium on the internal loans secured on the customs revenues. These latter revenues, figures of which for the past year are given elsewhere in this report, remain the sheet-anchor of Chinese Government finance, and all calls on them during the past year have been punctually and faithfully met. While most of the domestic loans secured on the customs are served from funds made over by the Customs 'Administration to the National Loans Sinking Fund Commission, some of the earlier ones are served direct by a department of the Customs itself.

In either case, the foreign Inspector-General of Customs has of recent years tended to become more than ever the trustee for the holders of domestic bonds, and his position and influence would be greatly impaired if the Government were to declare a moratorium on its internal loans. Even if a moratorium, which might be disastrous to China's credit, should eventually be avoided, it seems likely that some scheme for the funding of the internal debt, with a prolongation of the period of payment and a lowering of the rate of interest, will become imperative.

(b) Domestic Loans.

208. The increasing dependence of the Government on these domestic loans issues is illustrated by the fact that the total of 592 million dollars of such issues made by the Nanking Government from May 1927 to the end of 1930, was swelled to the extent of another 380 million dollars during 1931, making an aggregate of 972 million dollars (this figure must be regarded as nominal). This amount, added to the loans to the face value of 631 million dollars odd floated by the defunct Peking Government, make a grand total of some 1,603 million dollars. Of this sum, some 700 million dollars have been redeemed to date, leaving a balance outstanding of about 903 million dollars. After a steady fall since the beginning of the Manchurian crisis, Chinese domestic bonds in November reached the lowest levels ever recorded. Mr. Sun Fo, the leader of the Cantonese faction and head of the new Government, is recently reported to have described the financial situation as "hopeless" and stated that, since the establishment of the National Government five years before, the Chinese bankers had advanced 1,000 million dollars in domestic loans, which were now standing at an average of 30 to 40 per cent. of their face value.

The five loans to the value of 380 million dollars issued by the Government in 1931 were secured as to 80 millions on the increased customs revenues, 80 millions on the German portion of the Boxer indemnity, 80 millions on the salt revenues, 60 millions on the tobacco tax, and 80 millions on the surplus of the rolled tobacco tax, cotton yarn, and flour taxes. In addition to the above, a loan of 80 million dollars was authorised for flood relief purposes. It is understood that bonds were printed for 30 million dollars in respect of this loan, but owing to the political situation and the slump in all domestic bonds, had not actually been issued at the end of the year. In view of the difficulty of raising the necessary funds in any other way, the Government eventually decided to impose a Customs Flood Relief Surtax on all import and export duties. This surtax was to amount to 10 per cent. of such duties from the 1st December, 1931, to the 31st July, 1932, and thereafter 5 per cent. until the American Wheat Loan (see section I (5) of this report) was extinguished. The surtax was to apply to all goods with the exception of those imported articles on which the Chinese Government had in the exchange of letters attached to the Sino-Japanese Tariff Agreement of the 6th May, 1930, promised not to raise the duties for a period of three years. In addition, a surtax of 10 per cent. was collected on all railway passenger fares, for the same purpose, as from the 15th November.

(c) Foreign Loans.

210. As far as the foreign gold loans secured on the customs revenues are concerned, these were, as shown elsewhere, punctually met during 1931, in spite of the greatly increased cost to the nation in silver, a difficulty which is now to some extent counterbalanced by the collection of the import duties in terms of gold units (see under tariffs). The loans secured or partly secured on the salt revenues continued to be heavily in default as regards redemption payments though, apart from one half-yearly amortisation payment of £250,000 on the Anglo-French loan of 1908, the pledges given by the Minister of Finance on the 18th September, 1929, regarding payments to this loan, and to the Crisp Loan of 1912 and the Hukuang Railways Loan of 1911, out of the salt revenues, have been observed. No data are available as to the exact amount of salt revenues paid by the provinces to the Central Government during the past year. The detention of all the Manchurian salt revenues as the result of the Japanese assumption of control, formed the subject of a complaint by the Chinese Government to the League of Nations in November. The Canton Government also detained all the salt revenues under its control after it broke away from Nanking (see also under

customs). The position in regard to the railway loans shows no sign of improvement. In fact, the serious damage to the Peking–Mukden Railway (which almost alone of the Chinese railways has been free from the menace of civil war in recent years) and to the Shanghai–Nanking Railway, caused by Japanese action in Manchuria and more recently around Shanghai, has imperilled the future payment of these loans, hitherto the best-secured of the railway loans in China in which British nationals are primarily interested. The Tientsin–Pukow Railway continues to default in toto on the loans raised for its construction, in spite of the fact that it has been operating under one management and with through traffic restored through the greater part of the past year. The present situation at Shanghai will seriously affect the revenues of this line also, even if it should not come within the zone of actual hostilities. No payments have been made on the Canton–Kowloon Railway Loan of 1907, though the purchase of new sleepers and high-powered locomotives have recently greatly improved the running of this line.

(d) British Railway Material Debts.

211. In April 1931 Sir Miles Lampson sent in to the Waichiaopu a list of debts owing to British firms and nationals for railway materials supplied and not paid for as at the 31st December, 1930. These debts amounted to the large sums of (roughly) £1,100,000 and 11,500,000 Mexican dollars. The note forwarding this list only produced the stereotyped reply, to the effect that the liquidation of these debts must await a solution by the Commission for the Adjustment of Domestic and Foreign Debts, and that in the meantime a portion of the funds released by the British indemnity settlement was being used for the rehabilitation of the railways, which would have a beneficial effect.

(e) British Debts and Claims.

In a note, dated the 5th July, His Majesty's Minister also submitted to the Minister for Foreign Affairs a full list of all contractual debts and loans owing to British firms and nationals by the Chinese Government and its departments completed to the 31st December, 1930. These amounted at that date to £9,228,381 12s., 23,693,700 11 Mexican dollars and 21,663 50 gold dollars, including the debts for railway materials above mentioned, to which had to be added sums of £6,924,533 9s. 2d. and 4,765,296.86 Mexican dollars in respect of arrears of loans, issued internationally, in which the British interest is considerable. In addition, it was pointed out that there were other claims outstanding against the Chinese Government in respect of losses or damage suffered by British subjects and firms amounting to nearly 10 million dollars. The attention of the Chinese Government was drawn in this note to the high importance which His Majesty's Government attached to the liquidation of these debts at the earliest possible date. In reply, the Minister for Foreign Affairs was only able to state once again that the question would be raised at the next meeting of the Committee for the Adjustment of Internal and External Loans, without specifying when that meeting would take place. The Chinese Government have, in fact, taken no steps whatever to continue the debt consolidation discussions begun at the informal conference held at Nanking on the 15th November, 1930 (see paragraphs 318–322 of last year's report). When he took over the reins of Government at the end of the year Mr. Sun Fo is reported as having stated that even the small sum of 5 million dollars, which the Government had assured the creditor Powers was being annually set out of the increased tariff revenues to the consolidation of the internal and external debt, was nowhere to be found

(f) Establishment of National Economic Council and National Finance Commission.

213. In the spring of 1931 the Chinese Government issued regulations for the establishment of a National Economic Council. The inaugural meeting of this body was held at Nanking on the 15th November last, when the President, Chiang Kai-shek, chairman of the Executive Yuan, made a speech, saying that the council's first task would be the drafting of a three-year plan, covering the most urgent questions of economic development and having due regard to the financial resources available, beginning in 1932. This three-year plan was, it was

supposed, quite distinct from a highly ambitious and visionary ten-year plan for the industrialisation of the country, involving an enormous expenditure, put forward by the Ministry of Industry earlier in the year, but, in either case, the idea was based on the Soviet five-year plan, which has much impressed the Chinese mind. On the same day as this meeting was held the first meeting also took place of the National Finance Commission, a body composed, like the Economic Commission, of leading bankers and industrialists as well as officials and members of the Government. The functions of this latter commission are described as the adjustment of national finances, the examination of all military and civil expenditure, the examination of all bond issues, and the auditing and publication of the figures of Government receipts and expenditures; in other words, the establishment of the commission was designed to secure the issue of a regular budget and the holding of expenditure within approved appropriations. The establishment of such a body was in some sort an answer to a petition put forward by the Shanghai Bankers' Association, on whom the demands of the Government, as shown above, have become increasingly heavy, for the appointment of a committee to fix the budget, and to the criticisms of the Canton faction made at the negotiations held at Shanghai between the Nanking and Canton parties in October (the bankers were, in fact, trying to use the threat of "no money" to force the two parties to come to terms). The Minister of Finance, Mr. T. V. Soong, who individually had been made the target of much of this criticism, was probably anxious to shift some of the burden of responsibility for the nation's finances to other shoulders than his own. Moreover, in his annual reports on the national finances he had consistently urged the necessity for some proper budgetary system to co-ordinate the haphazard expenditure of different departments of the National Government (see paragraphs 325-331 of last year's report). At its inaugural meeting the National Finance Commission decided to reduce military expenditure to 18 million dollars a month (this was the figure agreed upon at the Disbandment Conference of August 1929) and administrative and party expenses to 4 million dollars, leaving a monthly deficit of some 13 or 14 millions, to be covered by issues of domestic bonds. Military expenses had previously averaged some 25 million dollars a month. This plan envisaged borrowing to the extent of 73 million dollars for the first six months of 1932, but it was stated that during that period more than that amount would be repaid to the holders of domestic bonds, so that no undue disturbance of the money market would occur. It remains to be seen what success will attend the efforts of these two commissions in collaborating to form a financial policy for the nation. The change of Government at the end of the year involved, as might be expected, an immediate change also in the leading members of the two commissions, as it did also in the incumbency of the Ministry of Finance, when Mr. T. V. Soong, with the retirement of the President, Chiang Kai-shek, his patron, gave way to a Shanghai banker, Mr. Huang Han-liang. The latter's position was, however, quickly made difficult by the political situation and the insistent demands of the new Government for funds, and it was expected that, with the almost inevitable return of General Chiang Kai-shek to power, Mr. T. V. Soong would also return to the Ministry of Finance.

(g) China and the League of Nations.

214. The Chinese Government have of recent years shown a growing inclination to turn to the League of Nations for expert assistance and advice in matters of development and reconstruction, such as public health, communications, harbour and river conservancy, and, particularly, finance. This fortunate tendency led to the visit to China early in 1931 of Sir Arthur Salter, Director of the Financial and Economic Section of the League. He was assisted by M. Frère, financial adviser to the Belgian Government, and Mr. Felkin. Sir A. Salter's extremely interesting and valuable conclusions as to how the Chinese Government might make a beginning in obtaining financial assistance, long since denied to it, from foreign markets were communicated to Sir Miles Lampson in private conversations, and were later supplied to the Foreign Office in the shape of copies of confidential memoranda. These views were, however, to a large extent dependent on the continued stability of the Government and the unity of the country, and would probably be subject to modification as the result of the grave situation prevailing in China at the end of the year. Very roughly stated,

Sir A. Salter's opinion was that eventually a scheme for the issue of an international loan, in national tranches, on the model of many recent European reconstruction loans, might be arranged in collaboration with, and approved by, the Financial Committee of the League, but that the days of foreign control and the employment of semi-independent foreigners, as the result of conditions laid down in treaty or loan agreements and similar contracts, were over, and that the Chinese Government were more likely to turn, of their own accord, to the League for assistance in obtaining the services of experts for carrying out necessary works of reorganisation, who would be employed by them and under their own unhampered control; in the meantime, while conditions were unpropitious for large issues in foreign markets, a beginning might be made with smaller loans for public utilities or industrial purposes. He also felt that the present highranking position of those of the national shares of the Boxer indemnity secured on the customs revenues, the proceeds of which were now for the most part devoted to various domestic purposes specified in the different indemnity settlements, was anomalous and tended to prevent the use of this-China's bestsecurity for the purposes of an external loan, and that these payments should take a lower position in priority, thus releasing this high-class security for loans for constructive purposes of greater importance to the nation. While realising the great economic value of the reorganisation of railway communications, he was not in favour of any wide-scale rehabilitation loan with first-class security involving payment of the outstanding obligations of the existing lines. He advocated, rather, that any financial assistance in the shape of a new loan, secured on the customs revenues, should be devoted to new construction and productive work. and should begin with one of the shorter railways, removed from the threat of civil war and consequent partition under several military commanders, where the Central Government would be more certain to be in a position to enforce its authority.

V.—TRADE.

215. The Statistical Department of the Chinese Maritime Customs has supplied the following preliminary statistics of the total net value of China's foreign trade in 1931, the figures for 1930 being also given for purposes of comparison:—

		Imports.	Exports.	Total.
		(In million	s of haikwan	taels.)
1930	 	1,309	895	2,204
1931	 	1,428	887	2,315

The figures for 1931 must be regarded as being little more than a rough estimate and will probably require amendment when fuller information has been received from all ports. As they stand they show an increase of over 100 million haikwan taels in the total value of trade, this increase being, however, entirely confined to imports. The average value of the haikwan tael in 1931 was 1/6–7/16, making the total sterling value of the trade approximately £176 million, against £208 million in 1930, when the haikwan tael was valued at 1/10–11/16. There was a further substantial increase in the balance of trade against China, the excess of imports over exports amounting in 1931 to 541 million as against 414 million haikwan taels in 1930, and there can be little doubt that this factor has contributed very materially to the difficult financial situation in Shanghai. The drain upon the country's resources resulting from the great preponderance of imports over exports has been accentuated by the depression prevailing in the Malay States, Java and other countries containing large numbers of Chinese settlers, whose remittances form the most important part of China's "invisible" exports and normally help to redress the balance.

216. The year 1931 was a period of exceptional difficulty for China's foreign and domestic trade. The extreme instability of the political situation, the constant menace of civil war, the frequent interruption of important lines of communication and the state of anarchy existing in many parts of the country tended to destroy confidence and to discourage commercial enterprise, whilst other factors have also contributed very materially to impede the movement of trade.

- 217. The low silver rates ruling throughout the year necessarily resulted in a great increase in the cost of all imported commodities in local currency, although this was partially offset by the reduction of producing costs in other countries, and as imports had also to bear the burden of the higher duties imposed under the new customs tariff, the result was to place many types of goods beyond the means of the buying public. In some cases this led to a marked falling off in consumption, and in others it encouraged still further the tendency to purchase goods of inferior quality in place of the better class article whose price had become prohibitive.
- 218. It might naturally be expected that the lower silver exchange rate, which had so depressing an effect on the import trade, would have had some compensating advantage by enabling China's exports to be sold at more competitive prices in foreign markets. To some extent this was, of course, the case, but owing to the industrial depression existing all over the world the demand for the various types of produce exported by China was so restricted that little advantage could be taken of this opportunity, whilst the unsettled conditions prevailing in China impeded the movement of cargo and rendered it difficult to arrange forward contracts.
- 219. The disastrous floods in Central China, besides causing enormous damage to life and property, also caused grave interference with both import and export business, and brought trade to a standstill throughout the vast area affected.
- 220. The anti-Japanese boycott in force during the second half of the year was not merely effective in crippling trade between Japan and China, but also had an unfavourable reaction on the general commercial situation, as the tying-up of the capital represented by the large stocks of Japanese goods held by importers and dealers added still further to the financial stringency, and finally the existence in Manchuria of what amounted in fact, if not in theory, to a state of war inevitably had a very prejudicial effect on all trade interests in that important market.
- 221. When considered, however, with special reference to British trade in China, the year 1931, in spite of the discouraging conditions described in the preceding paragraphs, had some redeeming features.
- 222. Although the important British distributing companies naturally felt the effect of the prevailing depression, they continued to show their ability to cope with a difficult situation, and on the whole the results of their year's trading must be regarded as reasonably satisfactory. The British American Tobacco Company report that the volume of their business, as represented by the quantity of cigarettes sold, was about the same as in the previous year, but that owing to the greater demand for cigarettes of the cheapest quality there was a considerable falling off in the cash value of their sales. The Asiatic Petroleum Company's trade suffered more severely, the decrease in sales, due to disturbed conditions and higher prices, being estimated very roughly at 30 per cent., and Imperial Chemical Industries had a fairly satisfactory year.
- 223. The local British shipping companies operating coast and river services derived a very substantial advantage from the boycott of their principal competitors, and the same remark applies to British cotton mills and other industrial establishments in China.
- 224. During the first nine months of 1931 the importation of goods from the United Kingdom was affected at least as severely as the trade of other countries by the fall in silver and the other unsatisfactory conditions already referred to. The position was, in fact, even more unfavourable for the sale of British goods than in the case of some of our competitors, as the higher cost of imported goods owing to the fall in the value of silver increased still further the tendency to make price rather than quality the first consideration. In the latter part of the year, however, two new factors—the anti-Japanese boycott and Great Britain's abandonment of the gold standard—effected a complete change in the situation, and resulted in a very marked increase in the demand for United Kingdom goods. Substantial orders for cotton piece goods, yarn and other commodities, of which Japan had previously been by far the main source of

supply, were transferred to the United Kingdom, and in machinery, metals and other manufactures the lower sterling exchange gave United Kingdom goods a great advantage over those of countries whose prices were still fixed on a gold basis. Owing to the generally unfavourable business and financial situation, the total volume of business secured by United Kingdom manufacturers as a result of these special factors, was probably not very impressive, and it must be admitted also that some anxiety is felt regarding the possibility of securing payment for all the goods ordered, but at least it may be said that in recent months Great Britain has been able to secure much more than her usual share of such trade as has been possible, and has gone a considerable way towards re-establishing, at least temporarily, her commercial position in China.

VI.—TAXATION AND TARIFFS.

(a) Taxation (General).

There is little to be added to the remarks made under this heading in paragraphs 342-350 of last year's report. Tax conditions usually reflect the unity or disunity of the country at any particular moment. The further the province concerned is from the central authority, the less likely it is to conform to the regulations and laws of the Government in matters of taxation. disturbed the political situation, whether from internal or external causes—as at the end of the past year—the less likely are the regular monthly subsidies and remittances from the Central Government likely to reach the provincial authorities at the due date, with the inevitable result that the latter become disposed to take the law into their own hands and to devise new local forms of taxation to make up the deficiency. Much fewer complaints of so-called illegal taxation reach the Legation from the consulates than formerly. Apart from general stagnation of trade, this is partly due to the fact that the treaty position was altered with the conclusion of the Anglo-Chinese Tariff Treaty of December 1928, and similar treaties with other Powers, and that British subjects are beginning to under stand that, as far as goods are concerned, the proper test is whether any particular form of taxation is levied in a regular and non-discriminatory manner under legislation of the central authority properly enforceable, but also because, outside the main centres of trade, where the writ of the Central Government may be said to run, they are more and more inclined to leave taxation troubles to their Chinese dealers and customers to face, until such time as the financial unification of the country becomes an accomplished fact.

(b) Special and Business Taxes.

226. The Central Government's intentions to collect a so-called "special" (or consumption) tax on certain classes of commodities, mainly of native production, and a business tax, of the nature of an income tax or of a graduated tax on the capital or turnover of business concerns, have so far hung fire and have not been carried to the extent of any uniform law nationally enforced. In fact, the National Government in April last decided against the imposition of the former type of taxation. While the name of "business tax" has been frequently and improperly used for taxes levied on goods at so much per unit, which are little else but the old li-kin or consumption taxes, foreign firms have not yet had to meet any organised attempt to collect from them any form of income tax in the proper sense of the word, nor, indeed, has any systematic effort been made hitherto to collect it from the Chinese themselves. In some provinces, the authorities have found so much difficulty in devising a method of assessment of this tax, that they have proposed to entrust its collection to the Chinese chambers of commerce, which will probably find means of their own for assessing what each firm ought to pay.

(c) Consolidated Tax.

227. The so-called consolidated taxes on cotton yarn, cement and matches are now collected by the Maritime Customs in the case of imported products in the same way as the similar taxes on wheat flour and tobacco, although these taxes were originally spoken of as excise taxes, with the result that the native-manufactured goods in these categories are protected to the full extent of the import duty.

(d) Tariffs (General).

228. As described in paragraph 351 of last year's report, a new import tariff, expressed in gold units, was introduced on the 1st January, 1931. Similarly, a new export tariff with many greatly increased duty rates was promulgated by the National Government on the 7th May and brought into force on the 1st June. So many other important factors have intervened since these tariffs were introduced to affect the trade of the country as a whole that it is difficult to estimate the influence of the new schedules on the trade in any particular commodity. While some of the revised specific export duty rates represent more than 5 per cent. of the value of the goods, other rates are still well below that figure.

(e) Export Duty on Fushun Coal.

229. When the new export tariff came into force a question arose as to payment of the increased export duty on coal by the Fushun collieries in Manchuria, owned by the South Manchuria Railway Company. At first the Japanese refused to pay any duty which was in excess of the amount stipulated under the Sino-Japanese Regulations of 1911, but before the end of the year it was learnt that they had agreed to deposit the excess duty into a special account until the question should be settled by negotiation. The matter affects the Kailan Mining Administration, who have to pay the enhanced export duty on their coal exported from Chinwangtao, although under a strict interpretation of their Amalgamation Agreement of 1912, which stipulates the amount of taxation of various kinds payable on their coal, they might equally find justification for claiming exemption from the increased export duty.

(f) Dairen Customs.

Another difficulty, typical of the Japanese attitude towards customs affairs in Manchuria, occurred over the cancellation by the Chinese Customs of the system of drawbacks on foreign duty-paid imports re-exported abroad as from the 1st April, 1931. The term "re-exportation abroad" was held to apply not merely to foreign countries, but also to the ports of Dairen and (until its restoration to China) to Tsingtao, as having a foreign status. With the abolition of coast trade duties in January 1931 the need for drawbacks on native cargo re-exported abroad disappeared, and the Chinese Government decided to withdraw also the similar privilege hitherto accorded to foreign imports. This had a considerable effect on the trade (chiefly in Japanese hands) in goods re-exported from Shanghai and other Chinese ports through Dairen into the interior of Manchuria, which were now forced to pay a second import duty at Dairen. So great was the pressure brought to bear by the Kwantung Government on the Dairen Commissioner of Customs in the matter that at the end of the year the Inspector-General of Customs had agreed to a provisional arrangement whereby goods shipped to Dairen and carrying proof that duty had already been paid once would be passed into the interior duty-free. This arrangement has not yet, however, received the sanction of the Nanking Government.

VII.—Customs.

(a) Revenues.

The total revenue collected by the Customs in 1931 amounted to 248,314,000 haikwan taels, or an increase of 67,744,000 haikwan taels over the previous year's collection. The largest increases were recorded at Shanghai (37,892,000 haikwan taels above the 1931 figures), Tientsin (10,115,000 haikwan taels), and Kowloon (4,078,000 haikwan taels). The increase at Dairen only amounted to 113,000 haikwan taels, while there was a decrease at Antung amounting to 452,000 haikwan taels. As shown in the section of this report under Trade, however, this increase of revenue expressed in silver, again, does not mean an increase in the volume of trade. The average value of the tael was the lowest recorded for many years past, while the introduction, on the 1st January, 1931, of the revised import tariff, expressed in gold units (see paragraph 351 of last year's report), and on the 1st June of the revised export tariff (see paragraph 354 of last year's report), largely contributed to the increase of

revenues. The small increase of revenue shown in the Dairen returns, and the actual decrease at Antung, reflect the large drop in trade caused by the crisis in Manchuria in the last quarter of the year. As before, all foreign loan and indemnity obligations, including the service of the Reorganisation Loan, have been met in full. The cost to the nation in silver was 119 million odd Shanghai taels, as compared with 91 million Shanghai taels in 1930, or 28 millions more. Similarly, the service, both interest and redemption, of all domestic loans and Treasury notes secured on the cancelled indemnities and on the additional duty has been met or provided for in full.

(b) Canton Customs.

232. Profiting by the lesson they had learnt under Yen Hsi-shan's administration in the previous year, the Central Government, on the declaration of independence of the Canton Government, agreed, upon the advice of the Inspector-General of Customs, though with considerable demur, to allow the Canton Government to retain the surplus customs revenues for their own use provided the revenues accruing from the original 5 per cent. tariff required for the foreign loan and indemnity payments were remitted to Shanghai as usual. This compromise was the means of maintaining, nominally at any rate, the integrity of the Customs Administration, which had been so seriously impaired in the previous year. It was, however, only reached after the Canton Government had instructed Mr. Maze to go to Canton as Inspector-General of Customs, and had subsequently offered this post to Mr. J. W. Stephenson, the Commissioner of Customs at Kowloon. This compromise continued in force till the end of the year, when, with the settlement of the differences between the Nanking and Canton factions in the Central Administration, regular remittances of all the revenues from the two Kwang provinces were resumed as from the 1st January, 1932.

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(c) Hong Kong Customs Agreement.

233. No further progress has been made towards the signature of the Hong Kong Customs Agreement (see paragraph 357 of last year's report). Private overtures were made by the Nanking Government to the Governor of Hong Kong with a view to the signature of the agreement after the Canton Government had declared its independence in June last, but were rejected by Sir William Peel, who felt that to agree to such a proposal over the heads of the Cantonese and pending the resumption of normal relations between Nanking and Canton would be tantamount to interference in China's domestic quarrels, and would eventually be resented by both parties. The proposal was evidently put forward at the time with the immediate object of damaging Canton's interests.

(d) Manchurian Customs.

234. Rumours were current towards the end of the year that, following the precedent of Canton earlier in the year, the Japanese intended to seize the Manchurian customs-houses and deal with them on the basis of remitting the loan quotas to the Central Chinese Government, while retaining the surplus for the purposes of the *de facto* Mukden Administration. The Minister of Finance stated that, if any such action were taken, he would close the Manchurian customs-houses, but at the end of the year no steps of the kind had been taken.

(e) Abolition of Intra-50-li Native Customs Stations.

235. The intra-50-li native customs establishments were abolished on the 1st June last. These had originally been entrusted to the Inspector-General of Customs to administer by virtue of the protocol of 1901, so that the revenue collected by these establishments might be devoted to the liquidation of the Boxer indemnity. The extra-50-li establishments had already been abolished with *li-kin* and other forms of internal and inter-port taxes at the beginning of the year. The revenues thus lost were more than compensated for by the imposition of the new Consolidated Tax (see paragraph 345 of last year's report) on certain commodities, which is really a part of the import duty, and by the raising of the export duty rates on native goods going abroad (see under Tariffs).

VIII.—THE BOXER INDEMNITY.

236. The Board of Trustees set up by the Chinese Government for the administration of the endowment arising out of the arrangements for the disposal of the British Boxer indemnity funds consists of ten Chinese and five British members. The names of the latter, who were appointed by the National Government in March 1931, are Sir W. W. Hornell, Mr. W. H. Donald, Mr. R. Calder-Marshall, Mr. Kenneth Cantlie and Mr. N. S. Brown. The Purchasing Commission in London, in addition to the Chinese Minister in London, and a representative of the Chinese Ministry of Railways (Dr. C. C. Wang was appointed to this post), consists of Sir Arthur Balfour, Sir Basil Blackett, Mr. W. T. Charter and Sir Ralph Wedgewood.

237. It is not possible as yet to specify precisely to what extent, and in what manner, the funds available to the Purchasing Commission in London for the purchase of material in the United Kingdom have been or are being expended, though it is understood that various purchases, principally of railway materials, have already been made. A system of allotment of the funds in fixed proportions to different departments of the National Government has been worked out which applies equally to the funds accruing direct to the Board of Trustees as well as to those in the hands of the Purchasing Commission. Under this system, two-thirds of the funds are to be used by the Ministry of Railways, and the remaining third divided between various river conservancies, the Ministry of Industry and the National Construction Commission. Numerous reports have appeared in the press of the allocation of varying sums to such objects, in addition to railway construction and rehabilitation and river conservancy, as the purchase of industrial machinery for Chinese-owned cotton mills, the training of Chinese students in foreign factories, &c.

238. Some question has arisen in regard to the relations between the Purchasing Commission in London and the Board of Trustees in China. The departments of the National Government, to whom funds have been allotted (see above) order their materials direct from the Purchasing Commission in London, without consultation with the Board of Trustees, so that the latter have no control over the expenditure of funds in the United Kingdom. The only part of the money so far being spent is that in the hands of the Purchasing Commission, and the Board of Trustees have no guarantee that the interest or amortisation on these funds, which are in the nature of advances to the departments receiving the materials, will be forthcoming. In the case of the railways repayment of such advances necessarily involves questions of priority vis-à-vis the bondholders whose bonds, which are in default, were secured on the earnings of the railway concerned. Apart from this point, in which British creditors are peculiarly interested, whether they are bondholders or suppliers of material not paid for, the attitude of His Majesty's Minister is that this Legation should as far as possible abstain from any interference in the affairs of the Board of Trustees, a body appointed by the Chinese Government, for whose activities it seems undesirable for us to accept any kind of responsibility.

239. The portion of the funds understood to have been allotted to the Ministry of Railways is as above stated to be two-thirds of the whole amount available from the British indemnity. As the Canton-Hankow line is, owing to insufficient progress in construction, not yet in a position to utilise the money, which is eventually intended to accrue to it under this scheme, for the purchase of materials in the United Kingdom, it appears to be the intention of the Chinese Government to sub-lend its share to other railways for purchases of material, these advances to be eventually repaid in China for use on the construction of the Canton-Hankow line.

IX.—AVIATION.

240. During the year China has made further progress in the development of civil aviation. A National Aviation Conference was held at Nanking in April, at which numerous proposals were adopted for the promotion and development of aviation. The conference concluded with a demonstration of both foreign and Chinese owned aircraft.

- 241. The Euro-Asian Aviation Corporation, which is a Sino-German concern, and was formed for the purpose of operating the Shanghai-Nanking-Peking-Manchouli section of the Shanghai-Berlin air service, was inaugurated on the 1st February. The corporation employs four Junker aeroplanes for the carriage of mails and passengers and four German pilots and nine mechanics. The service is bi-weekly and was formally opened on the 1st June with the departure of the first aeroplane from Shanghai. Unfortunately the Euro-Asian mail aeroplane which left Linhsi (Jehol) on the 2nd July for Manchouli with a German pilot and mechanic was damaged by rifle fire and forced to land in the neighbourhood of Lake Dalainor (Outer Mongolia) and was only located some days later by a second aeroplane of the service, which on coming down low was also fired on from the ground. The pilot of the captured aeroplane was severely wounded, and he and the mechanic were sentenced to ten years' imprisonment for espionage. Efforts were made by the German Legation in Peking by means of representations at Nanking and Moscow to secure their release and that of the aeroplane, which had not, in fact, obtained permission to fly over this corner of Mongolia. Finally, the aviators were released and arrived in Harbin on the 14th September, but the aeroplane has been still detained. The service was later suspended.
- 242. The Chinese National Aviation Corporation, which consists of Sino-American capital, and already operates the Nanking-Hankow Air Service, has opened a mail and passenger service between Nanking-Peking. The establishment by the corporation of a service between Shanghai and Canton is still under consideration. The Hankow-Ichang section of the Air Mail Service has been extended to Chungking and was inaugurated in October. The Sino-Japanese Joint Air Transport Company started a tri-weekly passenger service in December between Mukden and Harbin.
- 243. British aircraft have been well represented in China, and during the year substantial orders have been secured by British firms in the face of international competition. In Manchuria Messrs. Arnhold and Co. (Limited) representing De Havilland Aircraft Company (Limited) and the Blackburn Aeroplane and Motor Company (Limited) secured a contract in April for the delivery of nineteen Gipsy Moths amounting to £19,500. The Far Eastern Aviation Company (Limited) representing A. V. Roe Company (Avro-Lynx aeroplanes) signed a contract during the same month for the delivery of ten Avro (Armstrong-Siddeley engine) amounting to £25,300. In July in view of the fighting on the Peking-Hankow line the young marshal bought up all available aircraft in Mukden, including ten aeroplanes constructed in Japan on the model of the Nieuport machine, and at the time his air force numbered sixty machines, all of which, however, were not serviceable. The representative of Messrs. Arnhold and Co. (Limited) who were unable to compete with the Dutch Fokker Company's offer to the young marshal, which included the construction of an aeroplane factory at Mukden and the sale of seventy Fokker aeroplanes fitted with Armstrong-Jaguar engines, approached His Majesty's Legation in September for support in the sale of British machines. On the 18th September His Majesty's Minister impressed upon the young marshal the superiority of British planes, but the latter replied that the price was the stumbling block. In Amoy the Far Eastern Aviation Company were successful in securing a second contract at the end of 1931 for twelve aeroplanes costing £37,000. Elsewhere progress has also been made in the demonstration and sale of British machines.
- 244. The Central Government at Nanking have not been slow in developing their air force, but the tendency appears to be to purchase Junker aeroplanes in view of the extended credit system and the presence of German advisers in the capital. A contract was signed for twenty Junker aeroplanes, of which ten had arrived in July at a cost of 27,500 gold dollars each. Of the sum 25 per cent. was paid on the signature of the contract and the balance spread over a period of eighteen months to two years. It is also reported that a contract has been initialled, though not yet confirmed, between the Ministry of War and the German Junkers Aeroplane Company for the establishment of an aeroplane factory at Nanking with a capital of 3 million dollars, two-thirds of which will be taken up by the Ministry of War and the remainder by the Junkers Aeroplane Company.

245. China has been visited during 1931 by a number of aviators from Europe and America, including Miss Amy Johnson, Comte and Comtesse de Sibour, and Colonel and Mrs. Lindbergh.

X.—LEGISLATION.

(a) General.

246. The year 1931 showed no abatement of the stream of national and departmental legislatory enactments, upon which comment was also made in the annual report for the preceding year. A considerable proportion of this year's legislation, however, was in the nature of acts and regulations subsidiary or complementary to previous legislation, not yet put into force or awaiting further explanatory details as to the methods of enforcement. During the course of the year, for example, the requisite enactments were promulgated to put into force the following important laws: The Law for the Registration of Technical Experts of 1929, the Cinema Censorship, Company, and Preservation of Antiquities Laws of 1930, as well as Detailed Enforcement Rules for the Law of Publications (Press Law), which had already been promulgated and declared to come into effect on the 16th December, 1930. The publication of the Civil Code was also completed by the issue of the remaining two Books IV (Family Relations) and V (Succession), to become effective as from the 5th May.

247. Of other legislation enacted during the course of the year, the following are worthy of particular record:—

(b) Constitutional.

248. During the session on the 12th May of the National People's Convention at Nanking a provisional Constitution, which was subsequently formally promulgated on the 1st June, was adopted to meet the new conditions created by the declared emergence of the Chinese Republic from the military period to the period of political tutelage. Article 77 of this provisional Constitution provided that the organisation of the National Government of China and its component departments were to be separately determined, and a revised organic law of the National Government of the Republic of China, which was in effect an amended version of the original organic law of October 1928, was accordingly promulgated on the 15th June.

This organic law was, however, but short-lived, being superseded by the revised organic law of the National Government of China, adopted at the first plenary session of the 4th Central Executive Committee of the Kuomintang on the 26th December and promulgated in due form on the 30th of the same month. This revision of the organic law, the main object of which was to find some constitutional formula whereby the differences between the Nanking clique (Chiang Kai-shek, T. V. Soong, &c.) and the Canton faction (Wang Ching-wei, Hu Han-min, &c.) might be satisfactorily composed, *inter alia*, effectively reduced the position of the President of the Republic from that of practical Dictator, owing to his holding at the same time the position of president of the Executive Yuan and Commander-in-chief of the Army, Navy and Air Force, to that of titular head of the State for a limited term, with no political responsibility and without the right to hold any concurrent official position; the presidents of the five yuan were made severally responsible to the Central Executive Committee instead of to the National Government (i.e., the President) as before, and popular representation was introduced in a very modified form in respect to the election of one-half of the members of the Legislative and Control While the revision of June, therefore, only introduced minor amendments to the original organic law, this amendment of December entailed considerable fundamental reorganisation.

250. Article 80 of the provisional Constitution of May 1931 contained a proviso to the effect that the system of local government for Mongolia and Tibet would be separately determined according to local conditions, and in due course the foreshadowed legislation for Mongolia was duly promulgated (and came into

effect) on the 12th October in the guise of the Mongol League, Tribe and Banner Organisation Law, whereby, as the title implies, the old Mongol feudal or tribal system was adopted as the basis of government, subject, of course, to the necessary modifications and safeguards so as to reserve vital questions for decision by the Central Government of China.

251. Other constitutional legislation includes a series of laws regulating the division of the postal service in 1930 into the Directorate-General of Posts and the specialised Directorate-General of Postal Remittances and Savings Banks, as well as various ad hoc regulations, &c., defining the functions and composition of a number of newly-established organisations, such as, to name only the most important, the Bureau of Foreign Trade of the Ministry of Industry, the Navigation Bureaux, National Economic Council, National Finance Commission, and National Government Famine (Flood) Relief Commission.

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(c) Commercial.

(1) Banking.

252. A Banking Law was promulgated (and came officially into effect) on the 28th March for the regulation and control of banks, and was followed on the 1st August by the Banking Business Profits Tax Law and the Bank-note Issue Tax Law for the better utilisation of banks as a source of revenue.

(2) Companies.

253. The Company Law Enforcement Law of the 21st February made the Company Law effective as from the 1st July, on which date also came into force a corollary enactment, entitled Regulations for the Registration of Companies, issued by the Ministry of Industry on the previous day.

(3) Factories.

254. The date of enforcement of the Factory Law of 1930, originally fixed for the 1st February, 1931, was subsequently postponed to the 1st August, with the exception of article 13, dealing with the abolition of night-work for women, the operation of which was, in deference to representations from the interests concerned, specifically delayed for a period of two years.

255. A Factory Inspection Law for the inspection of factories in connexion with the Factory Law and its Enforcement Ordinance, both of the previous year, was promulgated on the 1st February and a mandate issued in due course for its enforcement as from the 1st October. In actual fact, however, this factory legislation is too radical and idealistic in comparison with existing conditions in China, and most of it remains, therefore, for the time being inoperative. It has, however, in the meanwhile been carefully studied by Dame Adelaide Anderson and M. Pône, of the International Labour Office of the League of Nations, who have compiled a memorandum of their views for the benefit of the Chinese Government and, in addition, discussed with the settlement authorities the question of its future applicability in the International and French Settlements at Shanghai.

(4) Shipping.

256. Particular activity has been demonstrated in respect of shipping legislation with the object, it would appear, of rounding off, as it were, the various aspects of shipping questions not properly covered by the Maritime Commercial (Trade) Law (promulgated on the 30th December, 1929, and put into effect on the 1st January, 1931), and the Shipping Law (Merchant Shipping Act) (promulgated on the 4th December, 1930, and put into effect on the 1st July, 1931), and of transferring the authority formerly exercised over shipping in addition to purely customs duties by the Chinese Maritime Customs, to the newly-established Navigation Bureaux. The original organic law for these bureaux, which were to be established at five centres, Hankow, Shanghai, Harbin, Tientsin and Canton—the last-named has not yet been established owing to the political differences existing between Canton and the Central Government at Nanking—with branches at other places as required, was promulgated on the 15th December, 1930, but their official inauguration was delayed till the 1st July,

1931, which, significantly enough, was the date determined for the coming into operation of the Law for the Registration of Ships and the Merchant Shipping Act of 1930, as well as of the three principal subsidiary enactments to the Shipping Act, namely, Regulations for Ships' Certificates of Nationality, Regulations for the Measurement of Ships, and Regulations for the Survey of Ships, all of which were promulgated on the 5th June, 1931. The powers of the bureaux were further extended by the Revised Organic Law of the Navigation Bureaux of the 26th September,

257. The question as to what extent this shipping legislation, which also includes the Ordinance governing Examinations of Pilots, Regulations for the Registration of Steamships and the Issue of Certificates, the Ordinance for the Examination of River and Sea Navigation Officers, and the Provisional Regulations for the Control of Seamen, of the 5th March, the 2nd May, the 7th May and the 1st October, 1931, respectively, is intended by the Chinese Government to apply at present, whether in whole or in part, to foreign as well as Chinese shipping, is, as is not infrequently the case with Chinese legislation, still rather obscure. There would, however, appear to be some hope of the question remaining dormant for the time being, except at Hankow, where the local bureau has adopted a rather truculent attitude.

258. Other legislation, under which term are included ministerial regulations and orders, issued during the year deals with such a wide range of subjects as control of narcotics, strategic and fortified zones, mining royalties, seamen's and other unions, various new loan issues, national, party and postal flags, budgets, student volunteers, arsenals, military academies, &c.

259. Under the heading of Legislation should also be included the mandate, and accompanying ordinance, of the 4th May, for the enforcement of Chinese jurisdiction over foreigners as from the 1st January, 1931, and the subsequent mandate of the 29th December postponing the said date of enforcement for an indefinite period.

XI.—PROPAGANDA.

260. Since the 1930 report there have not been, as far as is known, any fresh developments in the matter of organised Chinese press propaganda work by the National Government in foreign countries for the purpose of furthering national In China, portions of the United Press Service are made prestige abroad. available for the vernacular press in Chinese by the semi-official Kuomin News The latter also arranges for the issue of the Trans-Ocean Wireless Service, which is picked up by the Kuomin wireless installation at Shanghai, both to the foreign and vernacular press. It is understood that the salaries of the operators are paid by the Trans-Ocean Service, and that in return for the Kuomin Agency issuing the Trans-Ocean Service the latter telegraphs the Kuomin News to Berlin for redistribution there and elsewhere up to a telegraphic cost of 800 dollars per month. The Trans-Ocean Service is also said to pay a monthly sum to the Kuomin or Nanking Authorities and to be subsidised by the German Government. It is sometimes anti-League and generally anti-French; the Kuomin Service is openly propagandist according to the policy of the Central Government at the time; it does not use the British official wireless, and its English language service of Chinese news is intended primarily for propaganda among the foreign community and foreign correspondents. The United Press Service reaches China through the Chinese Radio Administration.

261. In Shanghai the official propaganda is under the control of the Publicity Department of the Shanghai Municipality headquarters, which is stated to have received 5,000 dollars monthly from party headquarters at Nanking for the promotion of the anti-Japanese boycott. Local Government departments dissociate themselves from official propagandist activities. It is believed that no financial support is given by the party organisation to the local boycott association. In Mukden during the summer the propaganda sheets issued by the Committee of Public Enlightenment became increasingly anti-Japanese, but ceased abruptly on the occupation of the city by the Japanese in September. In Kashgar no Chinese organisations exist for the furtherance of national propaganda abroad.

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- 262. The Law of Publications, which was promulgated at the end of 1930 laying down the conditions under which newspaper and magazines and books may be published and the penalties in the event of contravention, was supplemented in October 1931 by a set of explanatory rules drawn up by the Ministry of Interior in conjunction with the Central Kuomintang Publicity Department. This legislation has considerably strengthened the hands both of the Central Government and the party in checking anti-Chinese and anti-party propaganda in the press. At the beginning of the year the Tientsin newspaper, "Jen Min Jih Pao," was closed down on the grounds of the publication of articles critical of the People's Three Principles, whilst in April the Rengo Agency was denied the privileges of using the Chinese telegraph and mail facilities on the ground that it had frequently fabricated rumours likely to undermine the political stability of the country. The Chinese authorities stated that they would not lift the ban until the present Rengo representatives at Nanking had been removed.
- 263. Propaganda work undertaken by the Chinese Government and the Kuomintang through Chinese officials and residents abroad still appears to continue unabated and, as far as His Majesty's Legation is concerned, is chiefly concentrated in Malaya. The activities of the Kuomintang in that territory in particular are dealt with fully in a separate section of this report. Reports have also reached His Majesty's Legation to the effect that the activities of the Chinese consular officers at Penang and Calcutta are not above suspicion.

XII.—CLAIMS.

- 264. The whole question of outstanding claims of British subjects against the Chinese Government has been under consideration, with a view to the eventual presentation to the Chinese Government of a comprehensive list for examination, if possible, by a joint Sino-British Commission.
- 265. In the meanwhile a list is being prepared by His Majesty's Legation of all claims not yet presented to the Central Government, to be complementary to the list already forwarded to the Waichiaopu on the 14th May, 1925. Pending any necessary amendments the total of claims on this list would appear to be in the neighbourhood of 6½ million dollars, bringing the total outstanding claims in respect of loss or damage caused by rioting, brigandage, civil war, action of troops, &c., including the unpaid balance of the Nanking claims, to about 10 million dollars.
- 266. In the meanwhile the following claims have been separately presented to the Chinese Government during the course of the year:—
 - (1) On the 30th June: Claims of Messrs. Jardine, Matheson and Co. (Limited) and the British-American Tobacco Company (Limited), amounting in all to a little over 250,000 dollars for losses incurred through looting during the disturbances at Changsha in July 1930.
 - (2) On the 27th November: A claim for 258,287.68 dollars on behalf of the International Export Company (Limited) in respect of 41,452 head of sheep which had been confiscated, and subsequently auctioned in the spring of 1927 by the Tutung of Suiyuan, Shang Chen, while they were being pastured in the neighbourhood of Kweihua. This claim is incidentally quite distinct from a previous claim of 261,791.67 dollars already presented to the Chinese Government on the 12th April, 1928, in respect of another flock of sheep confiscated in Chahar during 1925 under the orders of Marshal Feng Yu-hsiang.
- 267. With regard to the settlement of the Nanking incident claims, pro rata payments are being distributed from time to time as funds are available, but progress has been very slow owing to the repeated and increasing delays on the part of the Chinese Government in handing over the due monthly instalments, of which only six, amounting to 1 million dollars (in addition to 100,000 dollars paid in June of the previous year), were remitted during the course of the year. The present position is that all the individual and smaller group claims have been settled, and payment has been begun of the main group and Government claims, of which about 1,250,000 dollars remains outstanding.

268. In addition to and apart from these claims for losses or damage incurred by British subjects in China, a list of the outstanding contractual obligations of the Chinese Government and its departments to British subjects and firms, compiled by His Majesty's Legation, was presented to the Chinese Government on the 5th July, 1931, in accordance with a suggestion made by the Chinese delegates at the conference held at Nanking on the 15th November of the previous year for the discussion of the problem of the settlement of the Chinese Government's contracted obligations now in arrears. The totals thus outstanding, in so far as British interests were concerned, as shown on this list which was brought up to the end of 1930, amounted to approximately £10 million, 26 million. Chinese dollars and 22 million gold dollars direct debts; to which must be added some £7 million, plus about 5 million Chinese dollars in respect of arrears of loans which were issued internationally, and in which the British interest is considerable.

269. Reference under the heading of Claims must also be made to the authority given by His Majesty's Government for the presentation to the Chinese Government of a claim for £1,000 on behalf of Mr. and Mrs. Thorburn as compensation for mental suffering and expenses incurred in their efforts to ascertain the truth in regard to the fate of their son John Hay Thorburn, who was arrested and brutally done to death by the Chinese military near Soochow during the first few days of June.

XIII.—Wно's Wно.

(Note:—A.R. = Annual Report. C.W.R. = "Who's Who in China," published by "China Weekly Review.")

Chang Chi. C.W.R., p. 3.

Born Chihli. Educated Paotingfu, and Tokyo. Early revolutionary. 1927 member of Central Executive Committee and Central Political Council. Vice-president Judicial Yuan 1928. In summer 1931 mediated between Nanking and Canton Governments. Elected chairman, Legislative Yuan, the 29th December, 1931.

Chang Ch'un. A.R., 1930; C.W.R., p. 11.

1931 resigned from Mayoralty of Greater Shanghai on the 10th December as a consequence of student disorders in Shanghai.

Chang Fa-k'uei. A.R., 1930.

1931, in April, on recrudescence of the anti-Chiang Kai-shih movement, made peace with Kwangtung and brought the Kwangsi generals to Canton. Took part in the quickly-abandoned anti-Nanking campaign in Hunan. Restored to membership of the Kuomintang in November.

Chang Hsiao-liang. A.R., 1930; C.W.R., p. 15.

1931 with headquarters established at Peking, as Vice-Commander-in-chief of the National Army, Navy and Air Force, controlled North China as far as the Yellow River. On the whole, maintained understanding with Chiang Kai-shih, whom he usefully supported by attending the People's Convention, Nanking, in May. Contracted typhoid fever in the summer. The 18th September onwards responsible for progressive peaceful withdrawal of troops inside the Wall without resisting Japanese advance. On retirement of Chiang Kai-shih, resigned post as Vice-Commander-in-chief, but appointed Director of the new Peace Preservation Committee, though omitted from new Government of the 29th December, 1931. Attempts to make him the scapegoat for Manchurian affair have so far failed, and position at end of year firm, though loss of Manchuria revenues embarrassing.

Ch'en Chi-t'ang. A.R., 1930; C.W.R., p. 46.

1931 with Ch'en Ming-shu in joint control of Canton during early spring. Suspect as former subordinate of Li Chai-sum (Li Chi-shen) and on the 28th April expelled Ch'en Ming-shu, denounced Chiang Kai-shih and later became member

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of the new Secessionist Government at Canton. Omitted from National Government the 29th December, 1931.

Ch'en Ming-shu. A.R., 1930; C.W.R., p. 58.

1931 head of Kwangtung Provincial Government till April, when he left Canton and remained loyal to Nanking in face of secessionist movement. End of September Nanking delegate to Canton for peace conference. Appointed garrison commander for Shanghai and Nanking areas with his XIXth Route Army (Cantonese) as garrison forces. Elected vice-president of Executive Yuan and Minister of Communications the 29th December, 1931.

Ch'en Shao-k'uan. C.W.R., p. 60.

Minister of Navy the 29th December, 1931.

Ch'en Yu-jen (Eugene Chen). C.W.R., p. 66.

1931 returned to China early in the year. Became Minister for Foreign Affairs of the new Canton Government. In June denounced Chiang Kai-shih to the foreign Powers. Mysterious visit to Japan in July, where he held informal discussion with Japanese Minister for Foreign Affairs. Became Minister for Foreign Affairs in Coalition Government the 29th December, 1931.

Chiang Chung-cheng (Chiang Kai-shih). C.W.R., p. 77.

From November 1930 onwards, increasing friction with Hu Han-min and the "pure" party, who regarded his understanding with Chang Hsiao-liang as a challenge to them. The 28th February, 1931, arrested Hu Han-min. In April split with Cantonese became definite and Sun Fo, &c., left Nanking. In May Chiang called People's Convention to bolster up the Government by giving it the appearance of popular backing against the party. In June commanded in person against Kiangsi Communists. Confirmed by Central Executive Committee as chairman of National Government and Commander-in-chief. Though unmoved by Cantonese denunciations he eventually resigned the 13th December in face of anti-Government student riots over Japanese-Manchurian question.

Chu Chia-hua. C.W.R., p. 105.

Appointed Minister of Education in Coalition Government the 29th December, 1931.

Chu P'ei-t'e. A.R., 1930; C.W.R., p. 110.

Re-elected Chief of General Staff the 29th December, 1931.

Feng Yu-hsiang. A.R., 1930; C.W.R., p. 126.

1931 during greater part of the year in retreat in South Shansi. Restored to the party in November in view of Manchurian situation. Elected to National Government Committee the 28th December, 1931.

Fu Tso-yi. A.R., 1930.

Made Governor of Ch'ahar early 1931 presumably to placate Shansi opinion. The 28th October created excitement by attempting to control all local revenues, but dissuaded.

Han Fu-ch'u. A.R., 1930.

1931 remained ostensibly loyal to Nanking. Commander of Main Reserve Forces against Shih Yu-san, July-August.

Hu Han-min.

1931 increasing friction with Chiang Kai-shih and governing clique led to his arrest the 28th February, in particular for his opposition to the calling of a People's convention and the proposed provisional Constitution; kept as a political prisoner till the 14th October, released as a result of Canton demands. Pleaded illness and remained at Shanghai during December, even after Chiang Kai-shih's retirement.

The 29th December, 1931, elected to Standing Committee of Central Political Council, but doubtful if he would co-operate with his two colleagues—Chiang and Wang.

Ku Wei-chun (V. K. Wellington Koo). A.R., 1930; C.W.R., p. 207.

Early part of year adviser to Chang Hsiao-liang. October became prominent as Chang's representative on the Special Foreign Affairs Committee for dealing with the Manchurian crisis. The 23rd November Acting Minister for Foreign Affairs (for Alfred Szê) after C. T. Wang's resignation.

Ku Ying-fen. C.W.R., p. 208.

Born Kwangtung 1875. In May 1931 denounced Chiang Kai-shih and associated himself with Ch'en Chi-t'ang in Canton. Member of the separatist Cantonese National Government till its dissolution.

Li Chai-sum (Li Chi-sen). A.R., 1929.

Detained at Nanking since spring 1929; released the 14th October, 1931.

Li Chin-lun (Frank W. Lee).

1931 October–November acted as Minister for Foreign Affairs till relieved by Wellington Koo. Resigned Political Vice-Ministry for Foreign Affairs the 31st December, 1931.

Li Tsung-jen. A.R., 1930; C.W.R., p. 248.

Like other Kwangsi generals, made peace with Kwangtung and in June joined separatist Kwangtung Government. Omitted from Nationalist Government the 29th December, 1931.

Lin Sen. C.W.R., p. 502.

March succeeded Hu Han-min as President of Legislative Yuan on latter's, "resignation." Became President of National Government the 28th December, 1931, with reduced powers in accordance with the amended organic law of the 30th December, 1931.

Liu Chih. C.W.R., p. 272.

1931 July-August in command Vth Route Army Group in the campaign against Shih Yu-san.

Liu Wen-tao. C.W.R., p. 287.

Born Hupeh 1894. Educated Paoting, Japan, Paris. 1929 Mayor of Hankow (conflict with Butterfield and Swire re bund frontage); appointed Minister to Germany the 17th November, 1931, arrived at his post the 30th December, 1931.

Lo Wen-kan. C.W.R., p. 294.

Minister of Justice the 29th December, 1931.

(Succeeded Eugene Chen as Minister for Foreign Affairs the 29th January, 1932.)

Ma Chan-shan.

First attained prominence by resisting Japanese in command of Heilungchiang forces on Nonni River November 1931. Acclaimed a "national hero." Promoted to general. By the end of the year he made his peace with the Japanese and joined the ranks of the Japanese "puppets."

Pai Ch'ung-hsi. A.R., 1930; C.W.R., p. 324.

1931 May joined Kwangtung National Government. August commander of one of three columns sent into South Honan as part of the offensive against Nanking, which was abandoned three days before Japanese entered Mukden the 18th September. Not included in Coalition Government, Nanking, the 29th December, 1931.

Shang Ch'en. A.R., 1930; C.W.R., p. 336.

1931 unpopular with Shansi generals. Resigned chairmanship of Shansi Provincial Government (replaced by Hsü Yung-ch'ang).

Shih Chao-chi (Alfred Sze). A.R., 1930; C.W.R., p. 345.

Chinese Minister to Great Britain. Distinguished himself in pleading China's case v. Japan at meetings of the League of Nations. Appointed Minister for Foreign Affairs in September, but did not proceed to his post.

Shih Yu-san. A.R., 1930.

1931, January and February, dissatisfied with settlement after 1930 rebellion, became centre of unrest and intrigue in South Hopei. July occupied Shih Chia-chuang without opposition. Rebellion failed through lack of support and his army dispersed. He himself escaped to Dairen, but returned to China in September.

Sun K'o (Sun Fo). A.R., 1930; C.W.R., p. 356.

1931. In April left Nanking with other Cantonese members of Government; proceeded to Canton, where he became member of the Secessionist National Government. In summer took part in negotiations for a settlement with Nanking party. On formation of new Government, he was allotted post of president of Executive Yuan (the 28th December, 1931), which post, under the terms of the new organic law, became vested with some of the attributes of a Prime Minister in a constitutional Government.

Sung Tze-wen (T. V. Soong). A.R., 1930; C.W.R., p. 264.

1931 resigned all posts, the 21st December, but returned to Ministry of Finance on the 25th January, 1932.

Tai Chuan-hsien (Tai Chi-t'ao). A.R., 1930; C.W.R., p. 366.

The 28th December, 1931, re-elected to presidency of Examination Yuan.

Tang Shao-yi. A.R., 1930; C.W.R., p. 369.

1931, end of May, joined Secessionist Government at Canton. The 29th December elected member of National Government Committee.

T'ang Sheng-chih. A.R., 1930.

1931 returned and lived in retirement in Honan, the 28th December, 1931, after Japanese crisis; appointed to presidency, Military Advisory Committee.

Tuan Ch'i-jui. A.R., 1930; C.W.R., p. 395.

1931, December, emerged from retirement in Tientsin to attend National Emergency Council re Japanese crisis.

Wang, Gaston (Lieutenant-General).

Ch'en Ming-shu's right-hand man in Canton. Chief of Staff, XIXth Route Army.

Wang Cheng-t'ing (C. T. Wang). A.R., 1930; C.W.R., p. 401.

1931, September, resigned position as Minister for Foreign Affairs as a result of criticism of his handling of the Wan Pao-shan, Korean massacres and Nakamura cases, and the student riots against the passive foreign policy vis-à-vis Japan in respect of the Manchurian situation (in course of which riots he was himself assaulted). December elected to National Government Committee.

Wang Ching-wei (Wang Chao-ming). A.R., 1930; C.W.R., p. 409.

1931 reappeared in Hong Kong in May and joined Secessionist Government, Canton. During summer and autumn took prominent part in negotiations between Canton and Nanking. The 28th December, 1931, elected one of the three members of Standing Committee, Central Executive Committee, member of

National Government Committee, and member of Central Political Council, but remained in Shanghai awaiting developments.

Wang Ch'ung-hui. A.R., 1930; C.W.R., p. 411.

1931, February, chairman of committee drafting new provisional Constitution, but in May fled to Nanking—anti-Chiang Kai-shih movement. Resigned presidency of Judicial Yuan and proceeded to Europe to sit in Hague Court.

Wu Ch'ao-shu (C. C. Wu). A.R., 1930; C.W.R., p. 436.

Minister to United States 1929 onwards; resigned 1931 owing to his affiliation to Canton party. President, Judicial Yuan, the 28th December.

Wu Chih-hui. C.W.R., p. 440.

Born Kiangsu 1864. Kuomintang elder statesman. During summer mediated between Canton and Nanking Governments. During Central Executive Committee debates on Manchuria crisis (December) caused a sensation and temporary crisis by accusing Cantonese of treachery.

Wu P'ei-fu. A.R., 1930; C.W.R., p. 446.

Still popular end of year; arrived at Peking from his retirement in Szechuan and was appointed to National Emergency Committee re Manchurian crisis.

Wu T'ieh-cheng. A.R., 1930; C.W.R., p. 449.

1931 mediator with Canton Government. The 21st August chairman of Commission for Overseas Chinese Affairs. The 29th December Mayor of Nanking.

Yang Shu-chuang. C.W.R., p. 426.

Resigned Ministry of Navy (succeeded by Ch'en Shao-kuan) the 29th December, 1931, National Government Committee. His resignation from Fukien Provincial Government not accepted, but allowed sick leave for two months with Fan Shen-tao acting.

Yen Hsi-shan. A.R., 1930; C.W.R., p. 474.

1930, the 22nd December, to August 1931 in Dairen, when returned to Shansi secretly at time of Shih Yu-san's rebellion, ostensibly for family reasons. As a result of Japanese crisis, restored to party (4th Party Congress), the 12th November. Member of National Government Committee, the 29th December, 1931

Yen Hui-ch'ing (W. W. Yen). A.R., 1930; C.W.R., p. 475.

Appointed Minister to United States, but proceeded to Geneva instead in 1931, December, as delegate to League of Nations.

Yu Yu-jen. C.W.R., p. 485.

1930, December, elected to Control Yuan chairmanship. 1931, the 31st December, re-elected to Control Yuan chairmanship.



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CHINA.

Annual Report, 1930.

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Sir M. Lampson to Mr. A. Henderson.—(Received October 13.)

(No. 1063A.)

Sir, Peitaiho, July 23, 1931.

I HAVE the honour to transmit to you herewith the annual report on China for the year 1930.

- 2. I much regret that the submission of this report has been delayed even longer than in previous years. I can only point out that I myself, with part of my staff, were absent from Peking almost continuously from the beginning of the year until the beginning of June, in connexion with my visit to Singapore and the negotiations on the subject of extra-territoriality at Nanking; during that time the completion of a work of this size and scope was beyond the powers of the skeleton staff remaining here, whose time was fully occupied in dealing with the current work of the Legation.
- 3. I am indebted for the preparation of the report to the members of my staff, most of whom have, as in previous years, contributed towards it; in particular, to Mr. Teichman, Chinese counsellor, for the sections dealing with the internal political situation and the negotiations on extra-territoriality; to Colonel Badham-Thornhill, military attaché, for the section on military operations; and to Mr. A. H. George, commercial secretary, who contributed most of the chapters on economic and related subjects (railways, tariff and taxation, maritime customs, aviation, trade-marks). With the exception of the sections on extra-territoriality and Sino-Russian affairs, the chapter on foreign relations was written by Mr. Stirling, second secretary, with the assistance of Mr. Harcourt-Smith, third secretary (sections on Canada, Belgium, Denmark and Siam, and part of the Russian section), and Mr. Cassels, assistant Chinese secretary (rendition of Amoy and Crown leases at Hankow and Kiukiang). Mr. Cassels is also responsible for the chapters on legislation and propaganda, and Mr. Harcourt-Smith for the section on Manchuria and the dependencies. The chapter on finance was contributed by Mr. Cockell, honorary attaché, and the general section on trade by Mr. Brett, commercial counsellor. Mr. R. H. Scott, of the Chinese secretariat, compiled the "Who's Who'" and the statement of the position with regard to British claims against the Chinese Government. I have, &c.

MILES W. LAMPSON.

12 DEC 1931

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Enclosure.

Report on China for the Year 1930.

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I.—INTERNAL POLITICAL SITUATION.

(1) General.

AS recorded in the last annual report, the year 1929 was one of almost continual civil warfare and political strife, but at its close the National Government, under Chiang Kai-shek, were still in the saddle, having defeated or out-manœuvred the various military leaders and political factions who had risen successively against them. The general outlook at the end of 1929 was, however, far from reassuring for the Central Government. In the south the rebel forces of Chang Fa-k'uei and the Kuangsi leaders were still in the field and threatening to invade Kuangtung. In the North the prospect was even more ominous. The revolted troops of Shih Yu-san had withdrawn to the North after their sudden coup at Pukou, which had so nearly caused the overthrow of the Nanking Government, but they were still unaccounted for and in occupation of the Lunghai Railway. The real attitude and intentions of the two over-lords of the North, Feng Yu-hsiang and Yen Hsi-shan, remained very much in doubt, except that it was evident that the former, in any case, was on the verge of an open rupture with Nanking. In general, the impression was growing that some big move was impending in the North, and that the spring of the new year would see the resumption of civil war on a large scale, this time between the National Government and the Northern leaders. During the year under review the storm in the North has burst, overshadowing all other political developments; but it has been successfully weathered by the National Government, who, at the close of the year 1930, find themselves, though financially exhausted, in a stronger position vis-à-vis their internal rivals than ever before.

- The first two months of the year were comparatively quiet, but the peace was that of the calm before the storm. It had from the outset been evident that Shih Yu-san's revolt was not an isolated outbreak, and that he had good reason to believe that powerful support would be forthcoming from the North. Behind him, as it subsequently turned out, were, in fact, arrayed the big battalions of Feng Yu-hsiang's Kuominchun and the Shansi army of Yen Hsi-shan. It was true that towards the end of January Marshal Yen had assumed the post of Vice-Commander-in-chief of the National forces, but this apparent absurdity was explained in Chinese eyes by his theoretical support of the National Government, in spite of his growing opposition to its President, Chiang Kai-shek. By the middle of February it was generally realised that a movement was on foot in the North involving a definite challenge to Nanking; and that in the South the anti-Nanking elements controlling Kuangsi were waiting to make common cause with the Northern leaders in the struggle against Chiang Kai-shek. Towards the end of the month the customary telegraphic warfare, which precedes every political crisis in China, culminated in the issue of a circular manifesto, over the signatures of Feng Yu-hsiang and Yen Hsi-shan and the other leading Northern generals, as well as those of their Southern allies, calling, without reference to the National Government, for the convocation of a Fourth Party Congress. Although this declaration professed to support a peaceful settlement, it was rightly interpreted, in view of its veiled repudiation of the Third Congress, held under Chiang Kai-shek's auspices in 1929, as a challenge to the President and a manœuvre on the part of Yen Hsi-shan to justify his position in the impending war; while the appearance of the joint signatures of Marshal Feng and Yen was taken as a public demonstration of the fact that the relations between these two leaders, the nature of which had been so long in doubt, were at last definitely cemented in an alliance against Nanking. It was, however, to be noted that the name of Chang Hsueh-liang was absent from amongst the signatures to this and similar Northern manifestos which now poured forth.
- 3. In the middle of March the Shansi authorities took the first overt action against Nanking by expelling from Peking the representatives of the National Government and appointing their own nominees to the telegraph, railway and other public offices. To this the Central party headquarters in Nanking replied by issuing a manifesto openly denouncing the Northern leaders as rebels, and declaring the intention of the Government to launch a punitive expedition for their extermination. About the same time Feng Yu-hsiang, who had been living in nominal retirement (under the protection or supervision of Yen Hsi-shan) in a village near Taiyuanfu, left Shansi and proceeded to Honan to resume personal charge of the armies of the Kuominchun. The die was thus finally cast for war.
- 4. At the beginning of April Yen Hsi-shan assumed office as "Generalissimo of the National Forces," and declared his intention of launching a "punitive campaign for the unification of the country," the names of the parties to be chastised being tactfully omitted. He also established his own Bureau for Foreign Affairs in the old Waichiaopu building in Peking, and claimed the right to sequestrate the revenues of the Tientsin custom-house (the story of the seizure of which is related elsewhere in this report). At the same time the leaders and representatives of the various anti-Nanking groups throughout the country, including, as well as the Shansi and Kuominchun groups, the Left Wing, "Western Hills," and Kuangsi factions of the Kuomintang, began to assemble in Peking for the purpose of discussing the establishment of a reorganised National Government in the North. But it was obvious that the militarists and politicians of these various groups and cliques, many of them old and bitter rivals in the recent past, had little common ground beyond their common enmity against Nanking, and that it would not be easy for them to effect any constructive combination. Thus, Yen Hsi-shan himself and the conservative Shansi leaders of his group had always been fundamentally opposed to the policies of the Left Wing of the Kuomintang Even the alliance between Yen and Feng was essentially a union of convenience, unlikely to stand any severe strain. And there were violently conflicting policies amongst the anti-Nanking politicians of the Kuomintang, especially between the Left Wing (or Reorganisationists) faction under the notorious Wang Ching-wei and the more conservative "Western Hills" clique, who had seceded from the main body of

the party after Sun Yat-sen's death owing to their refusal to co-operate with the extremists and the Communists, who controlled the tang from 1925 to 1927. Although, therefore, Chiang Kai-shek and the National Government were being assailed from front and rear, and facing half the country, both in the North and in the South, in arms against them, they enjoyed in the coming struggle the advantages, not only of a central position, a better equipped army, trained by German advisers, and the resources, financial and material, of Shanghai and the rich Lower Yangtze region, but also of a solid front against an unnatural combination of divergent interests. Apart from these considerations, the rival forces seemed evenly matched, and a military deadlock probable. But, from the outset, it was realised that the key to the situation was held by Manchuria, under Chang Hsueh-liang, who, though keenly wooed by both sides, showed every indication of adhering steadfastly to a policy of strict neutrality.

- As regards developments in the military situation, the month of April was occupied by both sides in getting their forces into position. The Kuominchun, with part of the Shansi forces, pushed down into Honan and occupied Chengchow, Kaifeng, and points further east up to and beyond Kueite on the Lunghai Railway. Chiang Kai-shek, apparently biding his time and waiting to be attacked, confined himself to occupying the southern section of the Tientsin-Pukou Railway in force with the National armies concentrated on Hsuchow and Pengpu. Other Shansi forces were in Chihli preparatory to an advance into North Shantung, the defence of which was entrusted to Han Fu-ch'u, one of the semi-independent generals formerly associated with the Kuominchun and now a supporter of the National Government, who had been driven out of Honan by the Kuominchun advance. On the Peking-Hankow Railway the Hupei forces, nominally loyal to Nanking, were entrusted with the defence of that province against any advance of the Kuominchun on Hankow from the north. The strategy of the two sides in the main theatre of war was obvious from the outset; Chiang Kai-shek's object was to roll back the main body of the enemy on Chengchow (the headquarters of Feng Yu-hsiang) and beyond, when he would be able to advance safely on Tientsin and Peking; while the Northern leaders aimed at Hsuchow and Pengpu on the Tientsin-Pukou Railway, the occupation of which would cut the Government forces off from Shantung and throw them back on Nanking and the Yangtze River.
- 6. Serious hostilities opened in May when, after some initial minor successes on the part of the "grey" semi-bandit forces which formed a screen in front of the main Northern armies in Honan, the National troops advanced in earnest and, coming into contact with the Shansi forces, drove them back in disorder along the railway to Lanfeng, not far short of Kaifeng. Here, however, the Government armies met the main body of the Kuominchun (who throughout proved themselves greatly superior to their Shansi allies as a fighting force) and were, in turn, thrown back on Kueite. These developments ushered in a prolonged period of trench warfare and military stalemate on this, the main battle front, Chiang Kai-shek repeatedly throwing his best forces into the attack, but failing to make any decisive impression on the Kuominchun, who were, in turn, unable to make any serious progress eastwards along the Lunghai Railway. This stalemate continued during the summer, in spite of a much talked of offensive by Chiang Kai-shek with ten divisions in the early days of June, the only result of which was to cause heavy losses to the troops of both sides, who began to show signs of war weariness. In Shantung, however, the Shansi forces advanced south successfully as far as, and beyond, the Yellow River and occupied Tsinan on the 24th June, Han Fu-ch'u withdrawing with his small army eastwards down the Kiaochow Railway. By the middle of July, therefore, the general outlook was none too bright for Chiang Kai-shek and the National Government.
- 7. In the meantime, developments had been occurring in the South, where the rebel forces in Kuangsi, abandoning for the time being their raids into Kuangtung, had turned north and invaded Hunan with the object of attacking the National Government in their rear. Advancing almost without opposition through Hengchow into the heart of the province, they reached the neighbourhood of Changsha early in June. Although it was reported that Government troops were being hurried down from Wuchang to stem the advance of the invaders,

Ho Chien, the fence-riding chairman of the Hunan Government, having apparently no desire to become seriously involved with either side, withdrew with his garrison forces a short distance to the west, thus allowing the Kuangsi troops to occupy the provincial capital almost without fighting. The Wuhan cities now appeared to be in imminent danger of falling into the hands of the prebels, who would then have been in a position to launch a vital attack on Chiang Kai-shek's flank and rear. But in the middle of June the news arrived that the Cantonese troops of Ch'en Chi-t'ang had invaded Southern Hunan. The Kuangsi forces were thus compelled to turn in their tracks to face the advancing Cantonese, and about the 20th June they evacuated Changsha, which was promptly re-entered by Ho Chien and his Hunanese.

- 8. While these hostilities in the south were dragging on without any definite result, and the armies of Chang Fa-k'uei and the Kuangsi and Cantonese generals were chasing one another fruitlessly round the borders of Kuangtung, Kuangsi and Hunan, the depredations of the bands of brigands and Communists in the Southern and Central Provinces were increasing to an alarming extent. Some of these bands, relics of the semi-Communist forces of the National Government during the Bolshevik phase of 1925–27, were organised into comparatively well-equipped "Red Armies," which were raiding villages and cities, murdering the officials, carrying off the richer inhabitants to ransom, and administering whole districts on Soviet lines. During June a number of important towns on the Yangtze were raided, including Tayeh, Shasi and With all available Government troops concentrated in the north against the Kuominchun, no city in Central China seemed safe from the depredations of these brigands and Reds. Towards the end of July it was suddenly reported that the Communist armies of Northern and Eastern Hunan had combined and were marching on Changsha. Two days later the news arrived that the Hunanese garrison had again evacuated the city, and that the Communists had entered unopposed and were looting and burning Government offices and foreign premises. Thus within the brief space of a few weeks the rich capital of Hunan Province was twice captured by enemy forces. But in this case, as in that of the Kuangsi raid, the occupation was of short duration. A few days later, on the 5th August, Ho Chien, who had surrendered the city, practically without fighting, to the excesses of the Communists, reoccupied it in similar fashion, the Communist bands passing on to other forays. Fortunately, thanks to the presence of British and other foreign gunboats, there was no loss of foreign life, and the damage to foreign property was less than might have been expected. But so feeble had been the resistance shown by the so-called Government forces against the Communists in Hunan that the capture of Changsha naturally gave rise to the gravest anxiety in regard to the safety of Hankow, with its large foreign community and big foreign trading and industrial establishments; and special measures were taken by the foreign Powers for the protection of their nationals in the event of an emergency arising. Considerable unrest and other indications of subterranean Communist activities were noticeable locally, but adequate measures were taken by the Chinese military authorities controlling the Wuhan cities to deal with the situation. Soon after the immediate danger passed with developments in the North
- 9. During the summer the interminable negotiations and arguments continued amongst the politicians of the Left and Right Wing factions of the Kuomintang assembled in Peking, accompanied by much coming and going between Taiyuanfu and the old Northern capital. Both the Left Wing (Reorganisationists) and Right Wing ("Western Hills" clique) combined readily enough in their denunciations of Chiang Kai-shek and the "illegal" Third Party Congress of 1929, but the controversy raged fast and furious over the question as to whether a fresh start should be made by going back to the First Congress held at Canton in 1924 or whether the validity of the Second Congress held under extreme Leftist and Communist influence in 1926 should be recognised. At last, in the middle of July, the rival politicians, spurred on by Yen Hsi-shan (who realised the equivocal nature of his position as long as he had no "Government" behind him), reached a sufficient measure of agreement to announce the convening in Peking of an Enlarged Plenary Conference, which was to include members of the Central Executive Committee both of 1924 and 1926, as well as representatives of all the groups concerned. On the 23rd July Wang Ching-wei, who

had been waiting for the adjustment of these difficulties, arrived in Peking, and on the 4th August he met Yen Hsi-shan at Shihchiachuang and discussed arrangements for the formation of a new party Government in Peking. On the 7th August the enlarged Plenary Conference opened their sessions, and a manifesto was issued explaining the party programme. All these declarations made at this time by Wang Ching-wei and his followers were moderate and unobjectionable in tone and expounded a variety of admirable principles, including the convocation of a People's Convention, the curbing of the power of the Tangpu (local party offices), and the reconstruction of the country in accordance with the doctrines of Sun Yat-sen. These activities were countered by a stream of propaganda from Nanking ridiculing the attempts of their party rivals to set up a Government in the North, making capital out of the unnatural alliance between the Left Wing of the Kuomintang and the "Northern Militarists," and charging Wang Ching-wei, Yen Hsi-shan and Feng Yu-hsiang with complicity with the Communists in the South.

- While these political discussions were proceeding in Peking, however, military developments were occurring which were destined to produce fundamental changes in the whole situation. During July, Chiang Kai-shek, apparently realising that he could not obtain a decision against the Kuominchun on the main front in Honan, changed his tactics and prepared for a drive up the Tientsin-Pukou Railway against his less formidable Shansi opponents with the object of recapturing Tsinanfu. In the latter part of the month a number of picked Nanking divisions, having been concentrated in Southern Shantung, began to push northwards up the railway and by parallel routes across country. From the outset of the new campaign the Shansi troops, who were in occupation of the province as far south as Taian, made but a feeble resistance and retired as the Government forces advanced. At the same time Southern reinforcements, transported by sea from Pukou, were landed at Tsingtao and sent west along the Shantung Railway in support of Han Fu-ch'u. At Chefoo, Liu Cheng-nien, who had maintained a discreet neutrality, indicated his adhesion to the side of the Central Government. In August developments rapidly ensued, and, in spite of heavy attacks launched as a diversion by Feng Yu-hsiang in Honan, the resistance of the Shansi army in Shantung began to crack before the converging advance of the Southern forces. By the middle of the month a general retreat of the Shansi troops from their positions south of the Yellow River was in progress, and on the 17th August the Government forces entered and reoccupied Tsinan. The Shansi army withdrew to, and remained for the time being on, the north bank of the Yellow River. But their defeat had been complete, large numbers of men and quantities of arms and ammunition and supplies had been captured, and their moral generally destroyed. It was noteworthy that the decisive victory which had resulted in the recapture of Tsinan had been gained by two Cantonese divisions, who had thus demonstrated the ability of Southern troops to put to rout a well-equipped Northern army.
- 11. By the beginning of September the whole outlook had thus been altered to the advantage of Chiang Kai-shek. The National Government were again in control of Shantung, where Han Fu-ch'u was installed as chairman of the Provincial Government at Tsinanfu; a large part of the Shansi army had been destroyed, and, except for the continued existence of the Kuominchun on their flank in Honan, there was little or nothing to stop the victorious Nanking forces from advancing and occupying Tientsin and Peking. No such advance was, however, made, and the reason for Chiang Kai-shek thus holding his hand soon became apparent when a further dramatic dénouement occurred.
- 12. As stated above, emissaries of both the Nanking Government and of the Northern allies had long been in Mukden working for the intervention on their side of Manchuria, while both sides had emitted a stream of propaganda claiming the support of Chang Hsueh-liang. In actual fact, the young marshal had so far maintained a strict neutrality, and, while nominally recognising the National Government, had carefully refrained from affording them moral or material support against their enemies. The only action the Manchurian authorities had so far taken had been to strengthen, in their own interests against possible future emergencies, their military garrisons at Shanhaikuan and in the adjacent intra-mural region up to the Lan River, which had long been occupied

by Fengtien troops. Whether the Mukden Government considered that with the collapse of the Shansi army the time had arrived to come out on the winning side, or whether they were not prepared to countenance the occupation of Chihli by Nanking forces, or whether Chang Hsueh-liang decided to intervene and put an end to the civil war through purely patriotic motives, may be arguable points. Possibly all these, among other considerations, were behind what followed. In August the young marshal, as though to evade the too persistent attentions of the emissaries of both sides, had proceeded to Hulutao to inspect the new harbour works there, and later on he had proceeded to the seaside resort of Peitaiho, which lies inside the Wall, but within the region controlled by the Fengtien troops. Here he had met His Majesty's Minister, and in the course of confidential conversations with Sir Miles Lampson towards the end of August he explained his attitude and gave a sufficiently clear indication of his intentions at a time when few outside his own circle had any inkling of what was to follow. He explained frankly that he had always been opposed to Yen Hsi-shan's venture and his attempts to set up a rival Government in the North, and that, while remaining loyal to the Central Government, he desired to see it reformed by the broadening of its basis to include representative elements in the North and other parts of the country and by the abolition of Tang (party) interference in administrative affairs; and he indicated that he was contemplating some form of intervention on the side of Nanking in about three weeks' time which would involve his taking over from Yen Hsi-shan control of Tientsin, Peking and the Province of Chihli.

- 13. In the meantime the Government builders in Peking were continuing their work in spite of the discouraging military prospects for their side. On the 1st September the Enlarged Plenary Conference adopted an Organic Law for the proposed new Administration, and appointed a Government Council under Yen Hsi-shan as chairman, which included also Wang Ching-wei, Feng Yu-hsiang, Li Tsung-jen, Hsieh Ch'ih, Chang Hsueh-liang and T'ang Shao-yi, the names of the two last being, of course, taken in vain.
- 14. Marshal Chang Hsueh-liang, after leaving Peitaiho to return to Mukden at the end of August, summoned a conference of the Manchurian leaders to decide on the course to be followed by the Government of the Three Eastern Provinces, with special reference to the proposed intervention of Mukden in the civil war. On the 18th September the decisive step was taken, and the young marshal issued a telegraphic manifesto deprecating the continuance of the civil war and calling for a cessation of hostilities and the submission of the various leaders to a settlement to be arranged by the Central Government. At the same time preparations were made for the transport of large bodies of Fengtien troops within the Wall. Yen Hsi-shan accepted the inevitable and proceeded to withdraw his armies back into Shansi. The politicians of the anti-Nanking combine under Wang Ching-wei did not immediately throw up the sponge, but replied to Chang Hsueh-liang's ultimatum by treating it as a peace appeal, commending him for his attitude, and urging the convocation of the People's Convention and the abolition of military dictatorship, the summoning of a "legal" party congress, the establishment of a democratic Government based on a bill of rights, and united action against the Southern Communists. At the same time, however, the Shansi officials and Kuomintang politicians, including Wang Ching-wei, departed hastily from Peking and withdrew into Shansi, where for a brief period they re-established their Enlarged Plenary Session of the party at Taiyuanfu
- 15. By the end of September the intervention of Mukden had been effective so far as concerned the occupation of the Peking-Tientsin area by Fengtien forces and the withdrawal of Yen Hsi-shan's army to Shansi. The Ist and IInd Armies of the North-Eastern Frontier Defence Force were sent inside the Wall, the former under General Yu Hsueh-chung, who established himself as garrison commander at Peking, and the latter under Wang Shu-ch'ang, who assumed office as chairman of the Provincial Government at Tientsin. At first there was some doubt as to the true meaning of the Manchurian move and the extent to which it was really meant to support Nanking. In due course, however, it became apparent that the young marshal's intervention was the result of some sort of bargain arrived at between him and Chiang Kai-shek in the sense that

the former would lend his support to the National Government on the understanding that the basis of the Administration would be broadened, the activities and interference of the tangpu in governmental affairs curbed and an amnesty granted to the Northern militarists and politicians associated with Mukden. During October a number of declarations were issued by Chiang Kai-shek on these lines, recommending a general amnesty for the political offenders, with the exception of Yen Hsi-shan and Ch'en Chiung-ming and the Communists, and favouring the early convening of a Fourth Plenary Meeting of the Central Executive Committee, the summoning of a People's Convention, the early reversion of the control of the Government to the hands of the people and the enactment of a provisional Constitution for the period of tutelage succeeding the successful conclusion of military operations. To these declarations the defeated allies replied that, as Chiang Kai-shek had thus publicly endorsed the programme for which they had been fighting, they would, in conformity with Chang Hsuehliang's "peace appeal" of the 18th September, withdraw their troops and await a peaceful settlement. These public declarations of the various leaders concerned represented, after the customary Chinese facesaving fashion, the nature of the understanding between Manchuria and Nanking and the abandonment of the conflict by the Northern allies. By the end of October such of the Kuominchun as had not gone over to the side of the Central Government had withdrawn with Feng Yu-hsiang from Honan into Southern Shansi, where, together with Yen Hsi-shan and his army, they awaited developments.

- 16. Chiang Kai-shek now left the front, where he had been personally conducting the campaign for some months, and returned to Nanking for the celebration of the National Day of the Chinese Republic on the 10th October. A few days later some sensation was caused by the news that he had been baptised as a Christian (Methodist) at Shanghai.
- 17. On the 9th October Chang Hsueh-liang formally assumed at Mukden the office of Vice-Commander-in-chief of the National Forces in the presence of a special representative of the National Government, thus ranging himself publicly on the side of Nanking and receiving from the Central Government formal recognition as the second military leader in the country after Chiang Kai-shek.
- 18. The situation in South China remained all this time more or less unchanged, the local campaigns carried on against the Kuangsi rebels by the Cantonese dragging on without decisive result. In the autumn a Yunnanese force invaded Kuangsi, nominally to co-operate with the Cantonese against the rebels, but in reality, as seems more likely, on some filibustering expedition of their own. Before the end of the year they had withdrawn, defeated and dispersed, into Yunnan.
- 19. On the 22nd September General Tan Yen-k'ai, an important figure of the Chinese revolution, died at Nanking. A successful scholar under the old régime and yet a staunch supporter of the Kuomintang from pre-revolution days, General Tan was generally respected by Chinese and foreigners, and came to be regarded, in his capacity as president of the Executive Yuan, as the senior member of the National Government, of which he became the acting head during the absences at the front and elsewhere of Chiang Kai-shek. He was accorded a State burial in a tomb near the mausoleum of Sun Yat-sen.
- 20. On the 9th October the Standing Committee of the Central Executive Committee of the Kuomintang issued a notice calling the fourth plenary session of the committee at Nanking for the 18th November. During the weeks preceding the meeting considerable anxiety was felt about the outcome in view of the fear of a serious split between the uncompromising stalwarts of the party, represented by figures such as Hu Han-min and President Chiang Kai-shek and those members of the Government clique who supported him in his policy of limiting the activities of the party and of fuller co-operation with other non-party elements in the government of the country, with special reference to the understanding reached with Chiang Hsueh-liang. In the result, however, these forebodings proved unfounded, and the meeting took place successfully from the 12th to 18th November. There was on this occasion no difficulty in obtaining a quorum, the only important absentees from the committee as constituted at the last party congress held in March 1929 being Wang Ching-wei, Feng Yu-hsiang

and Chao Tai-wen, all of whom had been dismissed from the committee. Amongst the "reserve" committee members who were chosen to fill these vacancies were Dr. C. T. Wang and Wang Po-chün, Minister for Foreign Affairs and Minister of Communications respectively. A number of important resolutions were passed at the meeting, including decisions to hold a "People's Convention" in May 1931 and to restrain the activities of the party offices and their interference with the judiciary, while arrangements were also made for certain reforms in the machinery of the Government and an extensive programme laid down for political and financial reconstruction.

- 21. Soon after the civil war had been brought to an end by the successful intervention of Mukden, it was generally known that Chang Hsueh-liang proposed to meet Chiang Kai-shek in person to discuss the details of the settlement and arrangements for the future. It was at first understood that the meeting would take place at Tsingtao. Eventually, however, the young marshal left Mukden on the 7th November, and proceeded to Nanking to meet the President and attend as an observer the Plenary Session of the Central Executive Committee there. This visit of Chang Hsueh-liang's to the capital, which lasted some three weeks, appears to have been entirely successful, and afforded a public demonstration of the reality of Mukden's co-operation with Nanking.
- 22. The occasion of the meeting of the Central Executive Committee at Nanking was further marked by special festivities, in celebration of the Government's victory over the Northern rebels and the "reunification" of the country, which the members of the Diplomatic Body were invited to attend. What was perhaps of more practical significance and political interest was the fact that the foreign representatives attending these celebrations were able to travel down from Peking to Nanking, in special cars provided by the Waichiaopu, by the Tientsin–Pukou Railway, which, except for brief intervals, had been closed to traffic by civil wars for years past.
- 23. Early in November Yen Hsi-shan and Feng Yu-hsiang issued public statements declaring their intentions to retire into private life. Marshal Yen carried this declaration into effect by withdrawing for a time to his native district of Wu-t'ai in Shansi; later, he proceeded secretly to Tientsin, whence, accompanied by his family and principal political associates, he subsequently left for Dairen en route for Japan. Thus passed, for the time being at any rate, from the political scene the figure of the "Model Governor" of Shansi, who had earned general respect for his efficient administration of that province since the days of the first revolution of 1911. Until 1927 he had been able to keep himself and his province out of the vortex of Chinese internal political strife. But, having eventually been drawn in, he was not a big enough man to save himself from being crushed between the hammer of the Kuominchun and the anvil of the National Government. At a comparatively early stage in the widening conflict between Feng Yu-hsiang and Chiang Kai-shek, it became evident that the geographical position and military policy of the Kuominchun were necessarily forcing the Shansi Government into taking sides either with or against them; with the result that Marshal Yen eventually found himself in the unnatural position of heading a rebel anti-Nanking combination, which included such incongruous elements as conservative Shansi, and the Kuominchun, and the Kuangsi and left wing factions of the Kuomintang.
- 24. Feng Yu-hsiang's precise whereabouts continued for some time to be a mystery, but it seems that he remained until the end of the year in a village in Southern Shansi.
- 25. Wang Ching-wei and his associates of the left wing of the party, after remaining for a while in Taiyuanfu, proceeded at the end of November to Tientsin, whence they also subsequently sailed for Dairen *en route* for Japan and Europe.
- 26. By December the Northern rebellion was thus finally liquidated. But there remained the question of the disposal of the Shansi and Kuominchun troops, still totalling some 50,000 to 100,000 men, who had withdrawn to within the borders of Shansi Province. Early in December Chang Hsueh-liang left Nanking to return to the North, proceeding in the first instance to Tientsin, where he

remained until the end of the year discussing with the Shansi and Kuominchun leaders, who visited him there, the problem of the disposal of their forces.

- 27. Amongst the decisions reached at the meeting of the Central Executive Committee in November was one arising from a motion of the Minister for Foreign Affairs (who had long been pressed on the subject by His Majesty's Minister), that immediate and effective steps should be taken by the Government for the suppression of the brigand and Communist bands in Southern and Central China. Considerable Government forces were, in fact, upon the restoration of peace in the North moved from the Northern provinces to the affected areas in the Yangtze Valley and further south; and in December Chiang Kai-shek himself proceeded to Kiukiang and Hankow to assume, it was announced, personal charge of the operations. Up to the end of the year, however, no concrete results had been obtained, and large areas in Fukien, Kiangsi, Hunan and Hupei remained in the hands of the brigands and Communists, who were continuing their attacks from the river banks on foreign and Chinese shipping on the Middle Yangtze between Hankow and Ichang. Moreover, behind them in Kuangsi, rebel forces were still in the field.
- The above review of internal political events in China during the year 1930 will sufficiently indicate the nature of the difficulties which the National Government has overcome and with which they are still faced. On the credit side we find the Central Government at the end of this eventful year ruling once more over a nominally united country with no major political enemies left in the field against them, and generally in a stronger position than at any previous period of their existence. On the other hand, the comparatively stable position now reached rests admittedly on the co-operation of two men (or the groups they lead or represent), who, between them, control the greater part of the country, namely, Chiang Kai-shek and Chang Hsueh-liang; and while the co-operation between these two leaders appears at present to be genuine and sincere, pessimists are not wanting who predict the early outbreak of another major civil war, this time between Mukden and Nanking. Moreover, the brigands and Communists, and also the rebel forces in Kuangsi, are still unaccounted for; and the major problem of the disbandment of the superfluous soldiery in the country, with special reference to the Kuominchun and the Shansi leaders and their troops in the North, has still to be dealt with. Nevertheless, the general outlook is greatly improved, and is certainly much better than could have been expected a year ago.

(2) Manchuria and the Dependencies.

- 29. Apart from the intervention of the Mukden Government in the civil war, and the Sino-Soviet negotiations following the Chinese Eastern Railway dispute, both of which questions are dealt with in separate sections of this report, the year was a fairly uneventful one for Manchuria. The young marshal's decision to throw in his lot with Nanking would appear to have had little repercussion in the Three Eastern Provinces, and though his abandonment of the traditional Manchurian policy of isolation is rumoured to have caused certain of the "Elder Statesmen" of Mukden some misgivings, there are no overt signs of hostility to his declared policy of co-operation with the Nanking Government.
- 30. Personally, by his assumption of virtual control over all China north of the Yellow River, Marshal Chang Hsueh-liang has greatly increased his prestige; while his investiture in October as Vice-Commander-in-chief of the armed forces of the republic raised him to the dignity of the second most important personage in the State. Moreover, the improvement in his health, already recorded in 1929, was maintained in 1930.
- 31. Internally, the year was not a happy one for Manchuria. The disorganisation of trade caused by the disastrous dispute with Russia over the Chinese Eastern Railway was further aggravated by the fact that the effects of the prevailing world economic depression began to make themselves felt in the three provinces during the early part of the year. For instance, the price on the London market of soya beans, the staple export of Manchuria, which in January 1929 had stood at £11 10s. a ton, fell rapidly during 1930, and by August stood as low as £7 5s. a ton. Violent fluctuations in the value of silver,

together with the chronic state of the provincial finances, still further contributed to the depression, which was reflected in numerous bankruptcies at Mukden, Harbin and other important towns.

- 32. During the course of the year there was a notable increase of banditry throughout Manchuria. Apart from the so-called "White Bands," whose activities are dealt with in another section, the ranks of the lawless were swelled by disbanded troops who had been unable to find employment. Their depredations extended even down into the vicinity of Mukden itself, where numerous highway outrages occurred. Towards the end of the year the Manchurian authorities showed signs of taking steps to cope with the menace.
- 33. Since the return of Marshal Chang Hsueh-liang from Nanking, the Kuomintang has been making vigorous efforts to bring Manchuria into the party fold. General Wu Tieh Ch'eng was sent up from Nanking as the Central Government's delegate, entrusted with the task of organising Tangpu in Manchuria. Acting on instructions from the Central Executive Committee, the Liaoning Provincial Government recently ordered all organisations to see that their subordinates were grounded in Kuomintang principles and induced to enrol as members of the party. Subsequently, some sixty leading officials, including the chairmen of the Kirin, Heilungkiang and Jehol Provincial Governments were sworn in as party members. Other signs of the increasing importance of the Tang in Manchurian affairs are to be found in the fact that the young marshal himself took the leading part in the recent celebration at Mukden of the anniversary of Dr. Sun's death, in the inauguration of weekly services in Dr. Sun's memory in Manchurian schools, and in the official opening in Mukden of the head Tang offices for Manchuria.

The South Manchuria Railway.

- 34. The year 1930 was not very satisfactory financially for the South Manchuria Railway. The resumption of traffic on the Chinese Eastern Railway deprived the Japanese line of much of the business which had been temporarily diverted to it during the crisis. The lack of demand for soya beans seriously affected the volume of export freights, while the trade depression and the fall in the value of silver, diminishing the purchasing power of the inhabitants of the area served by the railway, proportionately reduced the amount of import traffic. These adverse conditions, with their inevitable reaction on the budget of the railway, accentuated the policy of retrenchment which had been inaugurated by Dr. Sengoku in the previous year. Rigid economies and reforms were effected in the administration of the railway, while many of the less profitable subsidiary companies were reabsorbed into the parent concern, and henceforward operated on a diminished scale. Those of Mr. Yamamoto's grandiose projects, to which Dr. Sengoku was irrevocably committed, were developed but cautiously, while others were allowed to lapse. The construction of the Showa Steel Works was, for instance, under discussion throughout the year, but at the time of writing no definite decision would appear to have been made, and it is at least possible that, in view of the recent decline in the market price of steel, the whole scheme may be abandoned.
- 35. Apart from the building of certain light railways in the vicinity of Antung, all idea of further railway construction in Manchuria has for the moment at any rate been dropped by the company. Instead, it professes to regard with benevolence the various new Chinese railways already under construction or projected by the Manchurian authorities, on the grounds that, far from harming its existing business, they will provide more traffic than the new port of Hulutao will be able to handle, and that much of their freights will in consequence be diverted to Dairen.

Other Lines.

36. The termination of hostilities caused a certain increased activity in railway construction. The "North-Eastern Committee of Communications" set up by the Mukden Government has formulated ambitious projects for a network of railways to serve Hulutao, and for a number of strategic railways to be

built along the Sino-Russian border. The Hulutao network, which is to radiate from Lienshan (the junction for Hulutao on the Peking-Mukden line), is designed to tap the provinces of Jehol and Suiyuan, and to extend as far as the Amur River. Since, however, this programme envisages an expenditure of at least 90 million dollars, it is probable that, in the present state of Manchurian finances, these lines will not materialise for some years to come.

- 37. The construction of the Tsitsihar–Koshan line, which was interrupted by the hostilities, has been resumed rapidly, and trains are now reported to be running from Tsitsihar through Ningnien as far as Taianchen. The completion of this section, which henceforward will be treated as a branch line, has, however, for the moment been abandoned, and the main line is being extended northwards from Ningnien towards Noho. This railway, which is primarily being constructed for strategic purposes, will, it is proposed, be eventually continued as far as Taheiho on the Amur River.
- 38. The Taonan–Solun Railway is reported to be almost complete. Construction beyond Solun towards Hailar or Manchuli, is, however, unlikely to begin in the near future. The Peking–Mukden (Peiping–Liaoning) Railway contributes out of its earnings towards the building of the latter railway.
- 39. A through service, entirely over Chinese lines, was opened between Peking and Kirin, viâ Mukden and Hailung, on the 10th October.

Mongolia.

- 40. The growing economic independence of Mongolia upon the Union of Soviet Socialist Republics has caused a complementary diminution in intercourse with China. Trade along the Kalgan-Urga route during 1930 was of negligible volume, and the information regarding Mongolian happenings which filtered through to North China was correspondingly meagre.
- 41. In the middle of the year representatives of the Union of Soviet Socialist Republics and of the "Mongolian Republic" signed at Urga a series of conventions relating to various economic questions outstanding between the two countries.
- 42. A "Mongolian Affairs Conference" was held at Nanking from the 21st May to the 12th June, 1930, under the auspices of the Committee for Mongolian and Tibetan Affairs. It was attended by a number of delegates, who claimed to represent various different regions in Mongolia. A resolution was passed authorising the appointment of Deputies, who should reside in Mongolia, and regularly furnish the Chinese Government with reports on the conditions prevailing there; other resolutions were passed impressing upon the Mongolian people the need for protecting themselves, under Kuomintang guidance, from foreign imperialism; and urging the Nanking Government to devise schemes for the economic, educational and political development of Mongolia.
- 43. The labours of the conference are reported to have served no purpose other than that of angering the Mongolian authorities, who sent out circular telegrams, alleging that they had had nothing to do with the election of the so-called Mongolian representatives to the conference, who were persons unacquainted with Mongolian affairs and merely selected by the Nanking Government.
- 44. The Mukden Government showed signs, towards the end of the year, of making a belated effort to check Soviet penetration in Mongolia. Their action was apparently inspired by the fear lest Inner Mongolia should go the way of Outer Mongolia. Their efforts were reported, however, to have been somewhat lacking in tact, and consequently to have irritated the Mongolians

Sinkiang.

45. Sinking remains to all intents and purposes an antonomous State under the absolute control of Chin Shu-jen, chairman of the Provincial Government. The Central Government has so far wisely refrained from attempting to assert its authority in this remote part of China; its orders would

appear for the most part to be obeyed by the Provincial Government only when it is to the latter's advantage to do so.

- 46. The activities of "basmatch" raiders in the course of the year, and the hard terms offered to local traders by the Soviet sales organisation, somewhat impeded the development of trade between the province and neighbouring regions of the Union of Soviet Socialist Republics. Nevertheless, the economic life of Sinkiang is still largely dependent upon Russia, and Soviet penetration, particularly in the north of the province, showed a certain increase during the year. The ease with which the Union of Soviet Socialist Republics disposed of Manchuria in the Chinese Eastern Railway dispute, together with the completion of the Turk-Siberian Railway, seems to have opened the eyes of the Provincial Government to the helplessness of their isolated position in the event of the Soviet deciding to repeat in Sinkiang the tactics already used with success in Mongolia; the attitude, therefore, of the local officials toward the Soviet representatives in the province is for the most part one of nervous cordiality.
- 47. Relations between Great Britain and the Provincial Government, except for a few minor incidents, continued during 1930 to be friendly, and were materially improved by the arrival in Sinkiang of the first consignment of the 4,000 rifles and 4 million rounds of ammunition purchased from the Government of India. This consignment was escorted up from India by Colonel Schomberg, who nappened to be travelling privately to Sinkiang at the time, and was good enough to lend his services to the Government of India in this connexion
- 48. Owing to transport difficulties it was found impossible to deliver to Sinkiang in 1930 more than a small portion of the arms and ammunition ordered. It is hoped, however, that it will be found possible to deliver the balance in the course of 1931.

Tibet.

- 49. Early in the year, the strained relations prevailing between Nepal and Tibet aroused the anxiety of the Government of India. The tension had originally been caused, it will be remembered, by the indiscreet action of the Tibetan authorities in forcibly removing from the Nepalese Legation at Lhassa a Sherpa trader named Gyalpo, who claimed Nepalese nationality, and who had found sanctuary with the Nepalese representative. The man subsequently died as a result of ill-treatment which he suffered at the hands of the Tibetans.
- 50. At one moment there appeared to be a grave risk of this incident leading to an outbreak of war between Nepal and Tibet. The crisis, however, was happily averted by the counsels of moderation given to both disputants by the Government of India, but the reluctance of the Dalai Lama to make adequate apologies to the Maharajah of Nepal delayed the final settlement of the case.
- 51. In consequence of this delay the Government of India despatched to Lhassa early in 1930 Laden La, a Tibetan officer in British service, who was entrusted with the task of inducing the Tibetan Government to offer satisfactory amends to Nepal. Laden La, who arrived in Lhassa in February, conveying to the Dalai Lama a personal message and letter from the Viceroy, was successful in his mission, and an apology satisfactory to Nepal was despatched from Lhassa in March.
- 52. Meanwhile, China had not been slow to take advantage of the dispute as a means whereby to extend her influence in Tibet. Two successive emissaries of the Nanking Government, a Lama and a young woman of mixed Chinese and Tibetan blood, reached Lhassa early in the year, bearing letters from Chiang Kai-shek and other Chinese notabilities to the Dalai Lama.
- 53. The object of these visits was of course the reassertion of China's traditional suzerainty over Tibet; the Tibetan Government was exhorted to develop close ties with Nanking, in return for which they would receive armed assistance from China in their struggle with Nepal. The Dalai Lama was able to evade the dubious comfort of Chinese military support by informing the Nanking emissaries that the dispute with Nepal had already been settled through the good offices of the Government of India, and that the despatch of Chinese troops into his territory was therefore no longer necessary. But, inspired possibly by the

fear that the Chinese Government, if not conciliated, might effect the restoration of the Tashi Lama by a resort to arms, the Dalai Lama did in some measure respond to the overtures of Nanking. At all events, Laden La, during his three months' stay in Lhassa, had to report a marked increase in Chinese influence there; and it is not improbable that China would have increased her influence in Tibetan councils had not the Northern rebellion against Nanking compelled the premature return of the two Chinese emissaries to their country.

- 54. While in Lhassa, Laden La received from the Dalai Lama an invitation (which had been refused in 1929) for the political officer in Sikkim to pay a visit to the Tibetan capital in order to discuss with him various important outstanding questions. No white representative of His Majesty's Government had been in Lhassa since 1924, and British relations with Tibet had in consequence progressively deteriorated until the Gyalpo incident, when the mediation of the Government of India had provoked a marked recrudescence of Anglophile sentiment. His Majesty's Government, therefore, considering that the moment was propitious for improving our relations with Tibet, approved the projected visit, and Colonel Weir, accompanied by his wife, reached Lhassa on the 4th August.
- 55. During his successful stay in Lhassa, Colonel Weir was able to reach a settlement with the Tibetan Government on a number of points, such as the question of the wool monopoly and the supply of arms and silver to Tibet. Moreover, he found that the Dalai Lama, while anxious to secure the ratification by China of the Tripartite Anglo-Sino-Tibetan (Simla) Convention of 1914 governing the boundaries of Tibet, nevertheless concurred in the Government of India's view that a suitable moment had not yet arrived for approaching the Chinese Government about this question.
- 56. Colonel Weir, in the course of his stay, made it clear to the Tibetan Government that His Majesty's Government would never favour a renunciation of Chinese suzerainty, but would, on the contrary, welcome such improvement in Sino-Tibetan relations as would ensure peace and stability along the common frontiers of the two countries. He at the same time hinted that His Majesty's Government, while in no way desirous of interfering in Tibetan internal politics, would be glad to see the return of the Tashi Lama to his country. The Dalai Lama, however, did not respond to the suggestion that he should take the first step towards effecting a reconciliation, and at the end of the year the Tashi Lama was apparently still residing in Chinese territory and in receipt of a pension from the Chinese Government.
- 57. In other respects, the visit of Colonel Weir to Lhassa, which terminated on the 2nd October, was eminently satisfactory. By personal contact Colonel Weir was able to dissipate the suspicion in which he was held by Tibetan officialdom when he first arrived; and it may be said that his visit has placed Anglo-Tibetan relations on a better footing than they have known for many years past.
- 58. Apart from the visits, already recorded, of the two emissaries to Lhassa, China's policy towards Tibet in 1930 was, on the whole, less imperialistic than in former years, possibly as a result of her preoccupation with her own internal dissensions.
- 59. The Kuominchun, in order to participate in the offensive against Nanking, retreated from the Kokonor border early in 1930, and the Province of Ch'inghai, apparently to the relief of the Tibetan Government, again passed under the control of the Kansu Mahometan leaders. The only serious incident which troubled the Szechuan-Tibetan border during the year was a dispute which broke out between the two important lamasseries of Tache and Behru.
- 60. During the year, the Committee for Mongolian and Tibetan Affairs at Nanking, a Department under the direct control of the Executive Yuan, showed signs of increased activity, and announced in the summer that facilities had been granted for the education of a number of Tibetan students in China.
- 61. It is probably through the fostering of cultural relations and the spread of propaganda by returned students as well as by official emissaries, rather than by any resort to force, that China will seek to re-establish her influence in Tibet in the future.

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(3) Military Operations.

- 62. The report on military operations during 1929 closed with the remark that the situation during the year had been anything but tranquil. Little hope was held out that fighting would cease or that anything but chaos would reign during 1930. This pessimistic prognostication proved more than correct; fighting has been in progress throughout the year in one form or another. Main interest centred round the struggle of unusual vehemence which was fought out in Honan and Shantung between the Nanking Government and the Yen–Feng combination.
- 63. At close of 1929 Tang Sheng-chih commander of Vth Route Army (four divisions), though long suspected, had, by intrigue and fair words, persuaded Chiang, against his better judgment, to leave him in Honan. He utilised this opportunity to rebel. On the 4th December, 1929, he issued a circular claiming wide support, and at one time it looked as if his attempt to challenge the Government might assume serious proportions. The support he claimed was not forthcoming, and his rebellion ended as ignominously as it began. Tang, under advice from Yen, who was privy to all that was happening, threw up the sponge on the 12th January and disappeared eventually to reach Hong Kong about the end of the month.
- 64. Shih Yeh-san also chose this time to show signs of restlessness and had, in fact, been in open rebellion against the Central Government. He cut the Tsinpu Railway near Pengpu and was generally challenging the Government in Nanking. Chiang Kai-shih preferred to buy him off rather than disturb the plans he had in mind for dealing with the more serious struggle he saw coming.
- 65. The Government had long recognised that, sooner or later, they would have to fight to maintain their position.
- 66. Before proceeding to recount the military events throughout the year it might be well, for the sake of clearness, to set out in tabular form the various areas and spheres of influence controlled by individual leaders as they stood at the beginning of the year:—

Group: 1st and affiliated leaders. Commander: Chiang Kai-shih.

Area under control.—Kiangsi, Anhui, Chekiang, Kiangsu, Fukien, Shantung, Honan, Hupei, Hunan.

Remarks.—Hold of Central Government on Shantung was ephemeral.

Fukien nominally acknowledged the Central Government. Large areas of the province were in the hands of bandits.

Honan and Hupei were doubtful assets, *vide* below. Hunan has always been a doubtful asset and has always had Kuangsi leanings.

Group: 2nd. Commander: Feng Yu-hsiang.

Area under control.—Shensi, Kansu, Ninghsia.

Remarks.—Kuominchun had just retired from Honan and Hupei, but had every intention of returning in the spring.

Group: 3rd. Commander: Yen Hsi-shan.

Area under control.—Shansi, Hopei (Chihli), Suiyuan, Charhar.

Remarks.—Yen was undisputed master of these four provinces. The
Government writ ran, but only as a matter of expediency.

Group: 4th. Commander: Li Tsung-jen.

Area under control.—Kuangsi.

Remarks.—The possibility of this group making trouble is a continual menace to China. Permanent occupation by loyal Northern troops is the only real antidote to persistent revolts engineered by the Kuangsi party in the South.

Group: 5th. Commander: Chen Chi-tang.

Area under control.—Kuangtung.

Remarks.—The Kuangtung divisions have often been referred to as a 5th Group. With the temporary disappearance of Li Chai-sen, they have been more or less brought under Nanking.

Commander: Chang Hsueh-liang.

Area under control.—Manchuria and Jehol.

Remarks.—There were a few gestures, but, beyond nominally handing over the Chinese Eastern Railway negotiations, nothing tangible in the way of accepting the Nanking Government existed.

Nanking-Yen-Feng Operations.

Events leading up to the Struggle.

- 67. Internal politico-military events during latter part of 1929 and opening months of 1930 showed that the old cleavage, North against South, still survived as a dormant factor in the situation. The North have never taken kindly to rule by the South and never will.
- 68. Appearances to the contrary—ethnologically, geographically and temperamentally—the North and South are poles apart.
- 69. At the Disbandment Conference early in 1929 Yen Hsi-shan said little, but stopped long enough in Nanking to convince himself that Chiang, having got himself into power, intended to remain there. Yen realised it was only a matter of time and his turn for the melting-pot would come.
- 70. Feng, at this time, was nominally Minister for War, but soon realised that his post was a sinecure till such time as Chiang could force him out.
- 71. Yen returned to his province, kept up desultory conversations with Nanking, but spent his time plotting and intriguing with those whom he thought might be useful to him later.
- 72. Feng was nominally his prisoner, and Yen at one time conceived the audacious idea that he might be able to oust Chiang without bringing Feng into the picture. He intended to utilise his troops, but soon discovered that without Feng there was little cohesion in the Kuominchun. Other political events occurring at this time so alarmed Yen that he released Feng, who had all along maintained the view that nothing permanent could be got from Chiang till he was defeated in the field. Events proved his diagnosis of the situation was more correct than Yen's, who considered Chiang could be got rid of by political means.

Chiang's Activities.

- 73. Chiang Kai-shih had from the outset recognised the futility of supposing Feng could be got rid of by means other than force. Ever since the defeat of the Kuangsi clique in May 1929 he had been preparing for a struggle that he knew was inevitable. He engaged instructors from Germany, purchased aeroplanes and tanks as far as his resources permitted, and, generally, began the improvement of his divisions in every direction. Realising the weakness of the officer cadre in the past, he widened and improved the curriculum of the Central Military Academy at Nanking.
- 74. It was obvious he was preparing for a war that was to put an end to war.
- 75. Towards the end of January he began a gradual concentration towards the railway junction of Hsuchoufu. Here he and his advisers reckoned he would be in the best position to meet all onslaughts. On the 18th February the first clash occurred. Nanking troops attacked Sun Tien-ying, who, formerly in alliance with Shih Yeh-san, was now active on the Northern side.

Moves of the Rival Forces.

76. During early March and April a mobilisation of combatants, interrupted by occasional clashes of troops, in the forward area began :-

(a) Northern Combination, under Feng Yu-hsiang, began concentration towards Chengchow and Kaifeng on the Lunghai Railway.

The Shansi troops (less four army corps operating under Feng in Honan) occupied strategical points in Hopei and North Shantung, defending Peking and Tientsin.

(b) Government Forces were based on Nanking, Hsuchowfu and Hankow, on the Tsinpu, Lunghai and Pinghan Railways respectively.

(c) In the South, Kuangsi (Northern) and Canton troops, representing the Government, were engaged in desultory fighting during the year. These operations, with exception of a sudden incursion into Hunan, had little effect on the military situation as a whole.

Kuangsi's strength has varied throughout the year.

organisation is now very loose and irregular.

Operations as they affected the general situation are discussed under a separate heading.

Distribution of Rival Forces.

77. Government and Allied Troops: Commander-in-chief, Chiang Kai-shih.

Ist Army	Han Fu-chu Eleven divisions, including Fan Hsi-chi's XXVIth Army Corps	110,000	••	Shantung.
Hnd Army	Liu Chih	240,000	••	Kiangsu and Anhui.
Illrd Army	Ho Cheng-chun	170,000		Honan and Hupei.
VIIIth Route Army		80,000		Kuangtung and Kuangsi.
Artillery	Yang ChenFour regiments, twelve 10.5 cm. howitzers purchased from	6,000	••	Concentrated along railways.
Air Forces	Japan Chang Hui-chang Three squadrons of five planes each, later expanded to nine	3,000		Nanking, Hsuchoufu, Hankow Choukiakou

Notes.—Line of communication troops, garrison and other defence units brought Chiang's numbers up to 650,000, of which only about half did any fighting.

Nanking Air Force played a prominent part in the operations. On all fronts Chiang was able to

employ about fifty machines.

Armoured trains were employed on all railways. Twelve Carden-Loyd tanks reached the front, but did not get into action.

78. Northern Combination: Commander-in-chief, Yen Hsi-shan; Vice-Commanders-in-chief, Feng Yu-hsiang and Li Tsung-jen.

Ist Army	 Li Tsung-jen Seven weak columns			30,000		Kuangsi.
IInd Army	 D V. 1	•••		250,000		Shensi and Honan, with Cheng- chow as headquarters.
IIIrd Army	 Yen Hsi-shan Thirty-four infantry cavalry divisions		six	280,000	••	Hopei and North Shantung.
IVth Army	 Shih Yeh-san Twenty-four divisions			180,000		South Hopei and west Shan-tung.
VIIIth Army	 Five divisions		••	40,000		North Honan.

Notes.—Total about 800,000, of which only one-third were in action at one time.

The 1st Army, under Li Tsung-jen, had been fighting in the Southern provinces since the beginning of the year. Its operations, except for a short period when bandit operations enabled them to seize Changsha, had little effect on events in the main theatre.

The Hnd Army, or Kuominchun, were short of rifles and suffered from ammunition shortage.

Their big-sword companies did good service when they were able to close with the enemy.

The HIrd Army alone was properly equipped.

The IVth Army held their positions, but did little or nothing to assist the Northerners' cause.

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80. Order of battle and situation in the main theatre of war during first days of May :-

Government Armies.—General headquarters was established at Hsuchoufu.

Ist Army (Han Fu-chu). Headquarters had been established at Tsinan, (Shantung). At this time no Northern troops had penetrated into the Shantung Province. Units of the Ist Army were holding Tehchow (Tsinpu Railway, North Shantung), and were guarding the Yellow River crossings at Pingyin and Tunga (South-West Tsinan). Units were also stationed to west of Tsining.

IInd Army (Liu Chih). Headquarters had been established at Hsuchoufu (Kiangsu). The IInd Army was concentrated at Hsuchoufu, with an advance force stationed at Tangshan (Lunghai Railway). One cavalry division and two infantry divisions were at Pengpu (south of Hsuchoufu)

with advance units at Kwoyang (North-West Anhui).

IIIrd Army (Ho Cheng-chun). Headquarters had been established at Sinyang (Kinhan Railway). Advanced units were as far north at Kioshan. Two divisions were at Fancheng and Siangyang to guard the left flank.

Northern Armies. - General headquarters was nominally at Taiyuanfu, but fighting throughout, with exception of the Shansi army's operations in Shantung, was controlled by Feng, from Chengchow.

Ist Army (Li Tsung-jen). East Kuangsi and North Kuangtung.
IInd Army (Feng Yu-hsiang). Headquarters at Chengchou, with
advanced troops holding Kueiteh (Lunghai Railway), Pochou (North-West
Anhui), and Hsuchang (Pinghan Railway).

IIIrd Army (Yen Hsi-shan). Headquarters at Taiyuanfu. Troops, with exception of six divisions operating under IInd Army on Lunghai Railway, were distributed at strategical points in Hopei and along the Tsinpu Railway, between Tientsin and the north bank of the Yellow River.

Narrative of Events.

81. Offensive operations on the part of Nanking began with an attack along the Lunghai Railway from Tangshan area. This put them in possession of Mamutsi (Lunghai). In the meantime the Northerners' advanced troops from Pochou attacked towards Kwoyang and made some headway. Nanking counterattacked with two divisions, and drove them back west of Pochou to Luyi. On the Pinghan Railway front the right wing of the IIIrd Army crossed the Liuho (Central Honan) and occupied Linyinghsien.

82. Between dates, the 15th to the 21st May, the IInd Army alone captured in succession Kueiteh, Hsiapa and Liuho, owing to a poor defence on the part of and the "turning over" of Liu Mao-en's 66th Division, Northern troops, who were holding these places. On the Pinghan Railway the IIIrd Army was steadily advancing northwards and the leading units reached a point just south Here they came up against strong defence lines prepared by of Hsuchang.

Feng's troops.

- 83. Last weeks of May saw Chiang Kai-shih making desperate efforts to capture Langfang. The Northern combination line of resistance ran from the Yellow River north of Langfang, through Neikuan on the Lunghai Railway, Chihsien, Suihua, thence went to Hsuchang or Hsuchou (Pinghan Railway). The Nanking troops strove hard to break this line, but despite the assistance of aeroplanes and 10.5 cm. howitzers the attack failed. Sun Tien-ying succeeded in reoccupying Pochou, where he was besieged till the 15th July. Shansi troops operating down the Tsinpu Railway succeeded during this period in forcing Han Fu-chu's 1st Army to withdraw south of the Yellow River. The arrival of Kuangsi troops in Hunan at this juncture, threatening Changsha, served to create a situation not by any means favourable to Nanking.
- 84. A lull on all the northern fronts permitted Nanking to divert troops from Hankow to deal with the Kuangsi invaders. This show of strength combined with the advance northwards of three Canton divisions caused the speedy retirement of the invaders back to their province.
- 85. The last two weeks of June saw the launching of Nanking's second big offensive along the Lunghai Railway. General plan was to pin the Northerners

down in the vicinity of Lanfang, while a main force concentrated at Taikang (south of Lanfang) attacked in a north-west direction towards Kaifeng. For over ten days the struggle continued leaving Feng the victor. Once again the Kuominchun had proved themselves no mean adversaries. The Nanking main attack succeeded at one time in driving a salient into the defence lines about Tunghsu, only to be driven back once Feng had time to bring up reinforcements. On the 25th June, Shansi troops in North Shantung managed to capture Tsinanfu. The operations, far from enhancing the reputations of the Shansi troops, proved that they are in reality an army of sheep led by donkeys.

- 86. By the 1st July it was clear that the Kai-feng offensive had failed, but movements of troops indicated that Chiang Kai-shih had a new plan in mind. This was to contain on the Lunghai while he prepared for a strong offensive against the Shansi armies in Shantung. Feng, learning of the coming operations in Shantung, started operations towards Kueiteh (Lunghai Railway). His offensive took the form of a cavalry demonstration to the north of the railway while the main force endeavoured to outflank the Southerners' left flank south of the railway. Rain and mud much hampered the operations yet the attack managed to get within 3 miles of Kueiteh, where barbed wire and hastily thrown up defences brought it to a standstill.
- S7. On the 28th July bandit Communist troops, taking advantage of the absence of reliable troops from Hunan, took Changsha. This was a bombshell for Nanking, and all eyes were directed towards Hankow, where it was feared the Communists would bring off a similar *coup*.
- 88. In Shantung operations for the coming offensive towards Tsinan were making progress when Han Fu-chu, who thought he had contributed quite enough in holding up 70,000 men of the Shansi army for two months, suddenly announced his retirement.
- 89. Chiang Kai-shih was disturbed at this *dénouement*, but characteristically decided to send the 53rd Hunan Division by sea as immediate reinforcements. The arrival of this unit at Tsingtao and the persuasive efforts of General Ma Hung-kuei kept Han going long enough to bolster up the situation for a few days.
- 90. During the early days of August Feng continued his efforts before Kueiteh, achieved local successes, but failed to penetrate the defences. In Hunan and Kiangsi the Communist menace was brought under control and Changsha was reoccupied without resistance on the 5th August. The bandits stopped long enough to loot, plunder and kill and then disappeared.
- 91. Reinforcements from Ichang and Shasi bolstered up with unreliable elements from Szechuan were rushed down river for the protection of Hankow, but there is little doubt that lack of co-ordination amongst the bandits and the presence of foreign warships in the river had more to do with the escape of the town from capture than anything the troops did. On the Pinghan Railway front nothing of interest took place.
- 92. By the 12th August it was evident that Chiang's offensive in Shangtung had made considerable progress; the Shansi troops had abandoned all their forward positions, leaving behind most of their transport and all their stores. A rapid advance by the 61st Canton Division, by a track running parallel to and east of the railway track found Shansi preparing to evacuate Tsinan. Nanking aeroplanes (six) bombed and harassed the retreating mob. By the 17th the Shansi army were once more north of the Yellow River.
- 93. This victory had a big reaction on the general politico-military situation. It led to Manchuria's eventual entry into the arena on the 23rd September in the person of Chang Hsueh-liang, who, in consultation with Chiang Kai-shih, had previously determined to take a hand when the psychological moment arrived.
- 94. The latter half of August saw signs of activity on the Pinghan line; troop movements indicated that a new stroke against Feng was under consideration. By the end of the month the Lunghai and Pinghan fronts were in touch with each other and all available units from Shantung were in process

of transportation to their new assembly places. Han Fu-chu was detailed as guardian of Tsinan with four divisions.

- 95. Early September saw political events of great importance. Chang Hsueh-liang issued a circular calling upon both sides to cease fighting and suggested the calling of an all-party conference to settle differences. This was however, only a precursor to a military intervention; the precise significance of which was not grasped for some time. Hopei and Shantung north of the Yellow River were occupied by Mukden troops, and the Shansi remnants began a retirement back to their province.
- 96. By degrees it began to dawn on Yen that Chang Hsueh-liang's intentions might be anything but favourable to the Northern combination, but Chinese like he and his satellites hoped each day something would emerge that they could seize on as a sign that Chang Hsueh-liang had some deep game in hand. The Northern hopes vanished as each day made it clearer that Chang's conversations in Mukden with Chiang Kai-shih's representatives, over a long period, were not which side he would assist, but a matter of choosing the psychological moment to occupy Hopei with his troops.
- 97. During these happenings Chiang Kai-shih, the *moral* of his troops now in the ascendant, pressed his general offensive against Feng. Political events, the realisation that no further help could be expected from Yen's defeated remnants, and the lavish expenditure of money on the part of Chiang's emissaries quickly told on the Kuominchun *moral*. Lanfang was captured by Nanking. troops on the 29th September and Chengchow fell on the 6th October. Actually there was little fighting, but many of Feng's commanders preferred to remain behind rather than face the possibility of another winter in famine-stricken Shensi.
- 98. Thus ended a struggle which has really led nowhere. Unification, which was for Nanking the avowed object of the war, is still only a name, even should Chang Hsueh-liang continue to play second fiddle to Chiang Kai-shih. The country is bankrupt and things financial are likely to be chaotic for a long time to come.
- 99. By the end of October Manchurian troops on the Tsinpu line had penetrated as far south as Tehchow on the Hopei-Shantung border. On the Peking-Suiyuan Railway they had reached Tatung, and on the Pinghan line they had occupied as far south as Shuntehfu. Chang Hsueh-liang was appointed Vice-Commander-in-chief of the Nationalist Naval, Military and Air Forces with complete jurisdiction over Hopei, Shansi, Suiyuan and Shantung, north of the Yellow River.
- 100. The last two months of the year were marked by Chang Hsueh-liang's visit to Nanking in his capacity as Vice-Commander-in-chief, and his stay at Tientsin where he spent a month attempting to reorganise the Shansi army. He has only been partially successful in this, but affairs in the province are gradually assuming some degree of order after a period in which it seemed probable the troops would all turn bandits. Han Fu-chu in Shantung and Shih Yeh-san in North Honan are the two leading semi-independent militarists left in the North; it is a matter of speculation how the young marshal will deal with one or either of them should they think it worth while to attempt to improve their position.

Kuangsi and Kuangtung.

Inter-provincial Struggle.

- 101. Kuangsi troops under Li Tsung-jen have been practically in revolt against Nanking since May 1929, though fighting, since their abortive attempt to take Canton in December 1929, has been more or less confined to their own province.
- 102. Much movement took place during the earlier months of 1930, but there was really no fighting of importance. The Canton authorities in order to prevent

their own troops being transferred North, kept Chiang Kai-shih well primed with stories of attack and defence, many of which were largely figments of their own imagination.

- 103. Early in March the Kuangsi rebels seized Pakhoi and Limchow, two coast towns in south-west Kuangtung, which gave them the much-needed opportunity to procure fresh stocks of ammunition and supplies. The bandit menace was now beginning to be felt in north Kuangtung and west Kuangsi, with result that both sides found it necessary to despatch troops to threatened points.
- North and seized Changsha with the idea that the chaotic conditions then prevailing in Hunan would permit of their further advance to Hankow. Canton's action in sending three divisions to threaten their rear, and the fact that Hunanese troops under Ho Chien did not join up with them as expected, forced them to make back for Kuangsi as best they could. Harried and pressed during the march by the Cantonese divisions they became much disorganised and lost much of their fighting power. The bearing these events had on the general situation is touched on in the narrative dealing with the operations in the main theatre of war.
- 105. In June the situation in Kuangtung had improved so much that Chiang Kai-shih found himself able to direct the transfer of two of the best Canton divisions to the Northern front, viâ Hunan. Canton acquiesced with a bad grace, but from a financial point of view were glad to rid themselves of the responsibility of maintaining the troops.
- 106. Month by month the campaign dragged on with little doing except in the areas round Nanning and Kueilin. The titanic struggle going on in Honan was not without its effect on the local situation. Both sides tacitly agreed to await results up North before committing themselves to further fighting. In September and October Nanning was besieged by Yunnanese troops who, estensibly Nanking's allies, were really only interested in the fact that Kuangsi's possession of the city interfered with their opium sales. Chang Fa-kuei and Pai Tsung-hsi in the Kueilin area were being contained by the Cantonese 59th Division, and Kueilin was treated to a little bombing by Canton aeroplanes. Thus the year closed leaving things very much as they were four months before.
- 107. Both sides are weary of a business which they have come to realise cannot be settled by military means. The Kuangsi leaders are still in the field, but there is every reason to believe that the New Year will see negotiations for peace begun with Nanking paying the piper.

Bearing of Operations on General Situation.

- 108. On the 1st April, Li Tsung-jen, already in revolt against Nanking, was appointed Vice Commander-in-chief, and concurrently Commander of the 1st Army, Northern Combination, by Yen Hsi-shan. Li, though not a strong Radical himself, represents the military side of the Leftist movement in the Kuomintang. It was conjectured that his appointment as a Vice-Commander-in-chief of the Northern movement would create an impossible situation in Middle and South China for Nanking. Doubtful troops were expected to turn over, restoring the Kuangsi clique to their old position in Hankow. Events did not turn out as expected; Chiang's shekels proved more attractive than anything Yen Hsi-shan or Li Tsung-jen were in a position to offer.
- 109. From a purely military aspect the results were little better. Li's task as an ally of the combination was to accentuate the unsettled conditions in the South, press attacks on Canton and create a situation in Hunan which would force Chiang Kai-shih to divert troops from the main theatre of war. In these objects he failed, though his rapid movements and repeated changes of front caused Nanking some anxious moments.

Operations against Communist Bandits.

- 110. Feeding upon the opportunity presented by endemic civil war, Communist and bandit activities have been on the increase during the last two years. Specific outrages in January 1930 proved that communism, considered almost eradicated when Chiang Kai-shih removed the Government from Hankow to Nanking in 1927, had again become active.
- 111. Banditry has always been a scourge in China, but events of 1929 showed that a new movement, capable of much trouble, was taking root in the country. The Government have made spasmodic efforts to deal with the evil, but actual responsibility for wiping out the menace has been generally delegated to the provinces, who have always found it more convenient to ignore or buy off the bandits rather than make an honest effort to suppress them.
- 112. The struggle between the Yen–Feng combination and Chiang Kai-shih gave further impetus to the movement which, in early months of 1930, covered the whole of Kiangsi, Hunan and Hupei and was threatening to engulf other provinces as well. Yen Hsi-shan utilised the situation to the extent that he hoped the chaotic conditions in mid-China would force Chiang to transfer good troops south to deal with the outlaws. Chiang disappointed him, but now finds he is up against a movement which, having had time to organise, is now (November 1930) a much more formidable proposition than it was in the early months of the year.
- 113. In October Chiang, released from his task of subduing Yen and Feng, announced the beginning of his campaign to destroy and eradicate the Communists. By this time the whole of the Province of Kiangsi, with exception of Kiukiang, was in the hands of Red forces under Chu Teh and Mao Tse-tung. Changsha, which had already fallen in July to Red armies led by Ho Lung, was again in danger.
- 114. The provincial divisions having demonstrated their thorough worth-lessness, Chiang decided to send twelve regular divisions into Kiangsi and instituted an encircling movement against the bandit strongholds, the success of which depended on co-ordination of effort and the reliability of the troops. Employing untrained levies for a job requiring very special training, it is little wonder that Chiang's successes have been confined to the driving away of the bandits from the main arteries of communication. Adopting guerilla tactics, the bandits invariably managed to slip through cordons which are really little else than figments of imagination on the part of those responsible for furnishing Chiang with reports.
- 115. The closing months of the year find Chiang still reinforcing the infested areas. This decision is sound, but without permanent occupation of the areas by reliable troops it is difficult to imagine that the operations will lead to anything more than temporary suppression of the Communist menace.
- 116. The movement is now assuming proportions far beyond what might have, at one time, been measured in terms of fifteen Government divisions against a dozen groups of organised bandits. Chiang will have to give this rebellion still more attention if he is to carry out his intention to destroy and eradicate all subversive elements within the next few months.
- 117. From the foregoing narrative, it will be seen that the situation throughout the year has been anything but tranquil. Chiang Kai-shih, with advantage of a centralised position and command of financial resources denied to his enemies, has emerged victorious from a campaign which more than once threatened to engulf him and all his supporters.
- 118. The general military situation, as it stood at end of the year, is best illustrated as follows:—

Group: Four Eastern Provinces. Commander: Chang Hsueh-liang.

Area under control.—Manchuria, including Hopei, Suiyuan, Charhar, Shansi.

Remarks.—Shansi is at the moment in the hands of Shang Chen.

Feng's remnants are still in the province. Their reorganisation is reported as about to take place under control of Chang Hsueh-liang.

Yen has left the province and will no doubt proceed abroad. Feng's movements are uncertain, though he is credited as making for Europe viâ Urga.

Group: Nanking Government. Commander: Chiang Kai-shih.

Area under control.—Central and South China, with exception of large

areas under bandit control, Shantung.

Remarks.—Hold of Central Government over Szechuan, Kueichow, Yunnan and the newly-created Province of Hsikang is purely nominal. Each is exploited for the benefit of those who can maintain themselves in power.

The Kuangsi party, represented by Li Tsung-jen and Pai Chunghsi, still hold W. Kuangsi, though their power for mischief has been much reduced owing to the many vicissitudes they have experienced

during the past year.

Sinchiang, or Chinese Turkestan, is rapidly becoming Sovietised, though Nanking still claims some semblance of authority in the

province.

Kansu, Ninghsia and Shensi. These provinces formerly constituted the Kuominchun base. Shensi is now being administered by Yang Yu-chen on behalf of the Central Government. Since Feng's defeat Mahometan hordes, under one Ma Ting-hsiung, have gained complete ascendancy in Kansu.

Shantung is in the hands of Han Fu-chu, who has "North" leanings, but is at the moment receiving payment for upkeep of his

troops from Nanking.

Group: Bandit-Communist armies. Commanders: Chu Teh, Mao Tse-tung, Ho Lung and other less important leaders.

Areas under control.—Large tracts of Hunan, Kiang-si, Hupeh and Fukien.

Remarks.—Other provinces are also involved, but not to the same extent.

Little headway has, as yet, been made towards disposing of the bandits, though no less than fifteen divisions are now engaged in the work of

suppression.

An encircling movement on a large scale is being attempted against the Communist leaders occupying Kiangsi Province. It is doubtful whether anything more than a temporary abatement of their activities will be accomplished, though the Nanking Government have promised the complete extermination of all undesirable elements within two months. Chiang Ksi-shih himself has taken the field, indicating a sincere attempt to deal with the situation.

119. Comparing this table with that given in paragraph 4 of this report, it will be seen that there is really little change in favour of the National Government. Yen and Feng have been temporarily eliminated, but "balance of power" in the country pretty well remains as before. The spoils of war have gone to Mukden, who, without firing a shot, now hold all Yen lost. Bandits hold large tracts of territory in the South; present situation promises none too well for the Government. Chiang has certainly made some headway, but has not yet disposed of all the unruly and subversive elements in the country.

II.—Foreign Relations.

(1) Extra-territoriality.

120. During the year 1930 China came to closer grips with the major Powers on the question of extra-territoriality. It will be recalled that the Chinese Government had opened the ball in 1929 by addressing formal notes to the Governments of Great Britain, the United States, France, Holland, Norway and Brazil, expressing China's desire to have the restrictions on her jurisdictional

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sovereignty removed at the earliest possible date. (Of the other Powers still enjoying extra-territorial rights, Belgium, Denmark, Italy, Portugal and Spain had concluded in 1928 ambiguously worded treaties with China agreeing to surrender extra-territoriality when the other Powers did so; while, according to the Chinese contention, the Japanese and Swedish treaties had expired and were in course of being replaced by new arrangements with those Powers). The rest of the year 1929 had been occupied by the exchange of a long-range fire of correspondence on the subject between China and the Powers above referred to, until the issue on the 28th December by the Chinese Government of their mandate declaring that, as from the 1st January, 1930, all foreign nationals in China should abide by Chinese laws and regulations. At the same time, however, the Minister for Foreign Affairs had issued a press statement to the effect that the Chinese Government were prepared to consider and discuss within a reasonable time any representations from the Powers concerned in regard to this mandate. These developments, so far as Great Britain was concerned, had followed on an understanding of sorts reached with His Majesty's Government, who, in view of China's insistence on taking some unilateral step towards the abolition of extra-territoriality, had agreed that the 1st January should be treated as the date from which the process of the gradual abolition of British extra-territorial rights should be regarded as commencing in principle, and had expressed their readiness to enter into detailed negotiations as soon as political conditions in China rendered it possible to do so, with a view to the abolition of extra-territoriality by gradual and progressive stages. The step taken by the Chinese Government was thus capable of two interpretations, the one for home and the other for foreign consumption; so far as concerned the Chinese public, the National Government could claim to have carried out their declared intention of abolishing extra-territoriality by their own unilateral act; while vis-à-vis the foreign Powers it could be maintained that they had merely established a principle in a manner which left the door open for a settlement by negotiation within a reasonable time. To Chinese mentality, imbued with the national characteristic of make-believe, there was nothing abnormal in such a situation; indeed, according to Chinese theory, the treaty rights of the Japanese had long lapsed, though no apparent change had taken place in the status of Japanese nationals in China. To the practical Western mind, however, accustomed to deal with facts rather than theories, the situation created by the action of the Chinese Government was an abnormal and dangerous one.

121. Such was the background to this, the most vital, of China's international problems, at the end of 1929. On the 1st January, 1930, the Foreign Office handed to the Chinese Minister in London a further aide-mémoire defining the attitude of His Majesty's Government in the United Kingdom towards the Chinese mandate; His Majesty's Government assumed that, in issuing this mandate, the Chinese Government intended to make a declaration of the character indicated in the previous aide-mémoire (of the 20th December); on this assumption His Majesty's Government had authorised His Majesty's Minister to enter into detailed negotiations on the subject; but His Majesty's Government expected the Chinese Government to instruct the local authorities throughout China that the treaty stipulations affecting the status and privileges of British subjects in China remained in force until modified as a result of negotiations.

122. Early in January His Majesty's Minister left Peking for Nanking to initiate the negotiations with the Minister for Foreign Affairs, and, on the 10th January, Dr. Wang presented written proposals, in the form of an outline plan, in eight clauses, providing that, as from the 1st January, 1930, all British subjects in China should obey the laws, ordinances and regulations duly promulgated by the central and local Governments of China, and be subject to the jurisdiction of the Chinese modern law courts, for which purpose special chambers, with foreign legal advisers, would be set up for a period of two years at Canton, Hankow, Shanghai, Tientsin and Harbin. His Majesty's Minister refrained at the time from detailed comment, but emphasised that His Majesty's Government insisted, in accordance with the principle of dealing with the problem by evolutionary and progressive stages, on two points which were not provided for in the Chinese plan, namely, the reservation for a period of criminal

jurisdiction and the employment by the Chinese Government of foreign co-judges to participate in the trial of British cases.

- 123. While waiting for authority to present counter-proposals in the form of a skeleton British plan, on the lines of the programme so far formulated by His Majesty's Government, Sir Miles Lampson had the opportunity of sounding, we well as Dr. C. T. Wang, Dr. Wang Chung-hui and Mr. Hu Han-min, the two most influential civilian members of the Chinese Government, and the two most intimately concerned, as heads of the Judicial and Legislative Yuans respectively, with the problems at issue. While professing to accept the principle of gradual and progressive abolition, neither was at all receptive of the idea of the reservation of criminal jurisdiction, and both expressed the strongest possible opposition to that of foreign co-judges.
- 124. On the 3rd February His Majesty's Minister handed to the Minister for Foreign Affairs the British counter-proposals, in the form of an outline scheme in nine clauses, providing for the abolition of extra-territoriality by a gradual and evolutionary process along the lines of the transfer of jurisdiction by subjects, in the general order of (1) civil, (2) criminal, (3) personal status cases, the transfer of (2) not to take place until the experience gained in regard to (1) had demonstrated the safety of this further step; the civil cases to be transferred were to be limited to those classes in regard to which codes satisfactory to both Governments had been promulgated and enforced; and adequate safeguards were to be furnished, with special reference to taxation and interference with the persons, premises and shipping of British subjects, such safeguards to include foreign co-judges and some system of evocation.
- 125. In the course of the ensuing conversation, Dr. Wang, while criticising (as was to be expected) practically the whole of the British plan, took special exception to the proposals for foreign co-judges and the reservation, unless for a very brief and stated period of criminal jurisdiction. Eventually, however, he put what he termed a "hypothetical question," namely, whether, if China agreed to employ foreign co-judges, His Majesty's Government would agree to surrender criminal jurisdiction. His Majesty's Minister took due note of this suggestion, and so the matter was left for the moment.
- 126. It was only at the time of presenting the British counter-proposals on the 3rd February that His Majesty's Minister learned from his American colleague that the State Department had, ten days previously, handed to the Chinese Minister in Washington proposals which, by omitting the particular safeguards on which His Majesty's Government were throughout insisting, threatened to cut the ground from under his feet. A few days later Sir Miles Lampson received by telegram from London fuller details of the American action. It appeared that, on the 23rd January, the American State Department had handed to the Chinese Minister in Washington draft proposals for a settlement, though it was stated that these proposals were presented not as a definite offer, but rather as material for study. This American scheme embodied a number of safeguards (including the employment of legal counsellors and rights of evocation for five years), taken from the treaties concluded with Siam, Turkey and Persia; but its principal features from the British point of view were negative ones, in that there was no mention of the two major safeguards on which His Majesty's Government had throughout laid special stress, namely, the reservation of criminal jurisdiction and the employment of foreign co-judges.
- 127. On the 8th February the Foreign Office telegraphed to His Majesty's Minister commenting on the American action, speculating as to the extent to which it had weakened the position, and calling for Sir Miles Lampson's considered views as to whether it was still feasible to ignore this development and pursue the negotiations according to the original programme, or whether it would not now be necessary, to avoid placing themselves in an untenable position, for His Majesty's Government to accept the situation created by the American Government and concentrate on securing adequate minor safeguards in matters of detail. To this request for his views Sir Miles Lampson replied in the middle of February that he feared that the American action must seriously weaken his hand, questioning whether His Majesty's Government would be able to hold out on their original programme alone, and recommending that consideration be given to Dr. Wang's tentative offer of foreign co-judges in return for the

surrender of criminal jurisdiction, provided the other safeguards, including adequate duration of any arrangements made, could be secured. His Majesty's Minister also took this opportunity of raising the question of Shanghai, since his investigations on the spot there had led him to the conclusion that unless some specific reservation were made of the Shanghai area and of the areas of the other concession ports, it would be impossible, even after the transfer of civil jurisdiction alone, for any foreign-controlled municipality to function. This discussion of the question of the status of foreign concession and settlement authorities led to the subsequent incorporation as one of the main safeguards in the British proposals of the reservation of Shanghai and the larger ports.

128. These various points were considered by His Majcsty's Government, and at the end of February the Foreign Office replied concurring in the views put forward by His Majesty's Minister, i.e., that it was desirable to seek to exclude Shanghai from the scope of any arrangement for the immediate transfer of jurisdiction, and further that, though the prospects of success had been gravely prejudiced by the American proposals, it seemed worth while making an effort to secure foreign co-judges and rights of evocation in return for the surrender of criminal jurisdiction. With regard to the exclusion of Shanghai and other ports, it was true that His Majesty's Government had originally been opposed to dealing with the problem along what had come to be referred to as "geographical" lines (i.e., the abolition of extra-territorial rights in the interior and their retention at the treaty ports), as opposed to the system of handling it by categories of cases. But the weakening of the position in the latter respect by the action of the American Government had led to a reconsideration of the merits of the former method, which had from the outset been favoured by His Majesty's Legation.

129. His Majesty's Minister left Nanking in the latter half of February to return to Peking. Before taking leave of the Minister for Foreign Affairs he sounded Dr. Wang again on the subject of the latter's "hypothetical question." Dr. Wang was inclined to recede from his offer, on the grounds that his judicial colleagues were one and all adamant against foreign co-judges (thus giving the impression that the American proposals had done their work and that his offer was to be withdrawn); he referred, however, tentatively to the possibility of finding some solution both as regards handling the matter by specified classes of cases and excluded areas if a time-limit, which he indicated would have to be very brief, could be laid down.

130. On His Majesty's Minister's return to Peking he caused a new and more detailed British plan to be drafted, embodying the principles of the surrender of criminal jurisdiction and the retention of the three remaining major safeguards (foreign co-judges, rights of evocation, and the geographical exclusion of the Concession and Settlement ports), and incorporating the relevant provisions of the Siamese, Turkish, and Persian treaties adapted to local conditions, and such portions of the American and Chinese and other schemes as could be suitably worked in. A fortnight later this new plan was completed, in the shape of a draft treaty consisting, of a preamble and sixteen articles, and was submitted to the Foreign Office in the middle of March.

131. In the meanwhile the American Government had apparently been brought to realise, probably as the result of the comment it had aroused at Peking, that their experts had made a false move in the proposals communicated to the Chinese Minister in Washington in January, and on the 20th March His Majesty's Minister was informed by his American colleague of the willingness of the State Department to consider retracing their steps and pressing both for foreign co-judges and the reservation of criminal jurisdiction. Sir Miles Lampson thereupon explained to Mr. Johnson recent developments on the British side and read to him the new draft just prepared in His Majesty's Legation. Mr. Johnson expressed the opinion that these new proposals constituted a possible basis for a common draft on which he and His Majesty's proved the beginning of the re-establishment of a common front with the American Government. It was then and there decided to set to work to elaborate a joint draft, the production of which would, it was hoped, if approved by both Governments, induce the State Department to transfer their negotiations to

Nanking, and thus enable them to be carried on by the British and American Ministers in the closest contact with one another. While this unfortunately turned out to be a vain hope, agreement had by the end of March been reached as between His Majesty's Minister and his American colleague, so that they were able to submit to their respective Governments an agreed draft represented by the plan prepared in His Majesty's Legation with certain minor amendments designed for the most part to strengthen the various safeguards. In order to maintain as far as possible a common front with the other interested Powers as well, copies were at the same time communicated to the French, Japanese, Dutch and Norwegian representatives in Peking.

132. His Majesty's Minister was in Nanking again during April and May, but did not deal formally with the Minister for Foreign Affairs on the question of extra-territoriality during this visit. The matter was, however, ment oned in the course of conversation with Dr. Wang Chung-hui, to whom Sir Miles Lampson explained that His Majesty's Government were considering and preparing new draft proposals, but that they would not be ready for presentation to the Chinese Government for some time. Dr. Wang Chung-hui had readily accepted the position, admitting that the question was too intricate a one to be hurried over, but when, in response to his enquiry, Sir Miles Lampson had intimated that the new British proposals might include the principle of the surrender of criminal jurisdiction, but would certainly retain as essential safeguards that of foreign co-judges, Dr. Wang Chung-hui had expressed himself as strongly opposed to the latter, alleging that the "hypothetical question" had been put by the Minister for Foreign Affairs without the authority of any of his colleagues, none of whom approved of such a suggestion, which could not in fact possibly be adopted by the Chinese Government.

133. So far as the Chinese Government were concerned the negotiations were at a standstill from the spring of the year until the autumn, the comparative lack of interest in the question on the Chinese side being no doubt due to the outbreak of the civil war between the Nanking Government on the one side and Feng Yu-hsiang and Yen Hsi-shan on the other, which opened in April and came to an end, through the intervention of Manchuria on the side of Nanking, in September. The delay furnished a useful breathing-space, of which advantage was taken by His Majesty's Government to continue and carry to a conclusion the task of reaching agreement with the American Government on a common draft scheme for presentation to the Chinese Government. In the middle of April the Foreign Office had been able to inform His Majesty's Minister of their acceptance, subject to a few minor amendments, of the "Lampson-Johnson draft," and at the end of the month the State Department communicated to the American Minister their views in the form of a redraft, the main difference between the redraft and the original version being the reservation of criminal jurisdiction. In explaining their new attitude the State Department expressed themselves as prepared to accept the principle of foreign co-judges, though rather out of consideration for the British view than because they themselves attached importance to the point. The Department felt, however, that in opening the discussions with the Chinese Government, provision should also be made not only for evocation, but also for the reservation of criminal jurisdiction, which, as a result of the "surrender" made on the British side, had been deleted from the "Lampson-John draft" (ignoring the fact that this "surrender" had been forced on His Majesty's Government by the action of the State Department in submitting in January proposals conceding complete jurisdiction).

134. Sir Miles Lampson and Mr. Johnson thereupon set to work once more, this time in Nanking, with a view to producing further and, it was hoped, final recommendations for a common draft. This they in due course accomplished, working on the American redraft and the Foreign Office amendments with the result that they were able early in May to submit another agreed version to their respective Governments. As stated above, this latest draft differed from the original version mainly in the reservation of criminal jurisdiction; but since (as was natural) each revision led to the strengthening of existing and the incorporation of additional guarantees, the resulting document was overloaded with safeguards. His Majesty's Minister, in submitting it to the Foreign Office, recorded his doubts as to the desirability of holding back on criminal jurisdiction

which, together with the provisions for foreign co-judges, rights of evocation, and the exclusion of the principal ports, and of the other minor safeguards, made the proposals such as would almost certainly be unacceptable to the Chinese, even as a basis for discussion, thus involving a retreat on our part from the outset if the negotiations were to be continued at all. The Foreign Office concurred in Sir Miles Lampson's view, i.e., that the draft as it then stood was likely to be too unpalatable to the Chinese, and that the negotiations were unlikely to proceed on satisfactory lines until a basis was reached of offering to give up criminal jurisdiction in return for adequate safeguards in other directions. But they were prepared, in order to secure the great advantage of a united front, to take, in the first instance at any rate, the same stand as the American Government, seeing that the latter had retraced their steps and now desired to reserve criminal jurisdiction.

- 135. Discussions between London and Washington ensued, and a final version (known as the draft of the 4th June) was eventually produced, which, after some further minor amendments had been introduced, was adopted as representing the common views of the two Governments. All the safeguards which had been considered were contained in this draft, including the reservation of criminal jurisdiction, but it was provided that this point might be reconsidered after five years' experience of the working of the agreement. A further safeguard introduced into the preamble provided that the agreement was not to come into force until the Chinese Government had demonstrated their ability to give effect to its terms throughout China.
- 136. There were no developments in the summer except that on the 5th July the Minister for Foreign Affairs at Nanking conveyed to His Majesty's Minister (who was spending the hot weather at Peitaiho in the North) a message urging the imperative necessity of the two Governments resuming negotiations and arriving at a definite and satisfactory settlement at an early date and pressing Sir Miles Lampson, if the views of His Majesty's Government had crystallised into definite proposals, to put forward such proposals and continue the discussions in the same friendly and sympathetic spirit as heretofore. To this message, which was probably in the nature of a gesture connected with the internal political situation, Sir Miles Lampson, after consulting the Foreign Office, replied that it had always been his intention, subject to political contingencies, to spend the month of September in Nanking in order to continue the discussions already begun on various outstanding questions; that, His Majesty's Government in the United Kingdom having nearly completed their study of the extra-territoriality proposals, he, His Majesty's Minister, expected to receive detailed instructions before his departure from the North, and that he hoped to make such progress with the negotiations as the general political situation in China would permit.
- 137. During August the question arose, in view of the fact that the civil war between the North and Nanking was still raging, as to whether any further discussion of the surrender of extra-territoriality was not premature in view of the existing conditions in China. The American Government argued that there was no opportunity for negotiations at such a time, and urged His Majesty's Government to postpone any further action in the matter. The Foreign Office, however, concurred in the strong opinion of His Majesty's Minister that as a general principle it was unwise to hold up the implementation of a predetermined policy owing to the flux of political events in a country like China, and that in any case no harm could come out of the presentation of the proposals, since, in the most improbable event of the Chinese Government accepting them, His Majesty's Government would secure all the safeguards and reservations which they could possibly desire, while, on the other hand, if, as was almost certain, the proposals were rejected, no harm would have been done and His Majesty's Government would at any rate have made good their promise to table proposals of some kind.
- 138. His Majesty's Minister eventually left the North on the 5th September, having received a few days before final instructions from the Foreign Office, making certain last moment amendments, mainly of a formal character, in the agreed draft. On the 11th September Sir Miles Lampson handed to the Minister for Foreign Affairs at Nanking His Majesty's Government's proposals in the

form of a draft treaty and protocol (which took the place of the preamble in the original draft) providing for the gradual abolition of British extra-territorial rights in China. It being apparent that the document was too lengthy and involved to be immediately considered, further discussions were adjourned to enable the Minister for Foreign Affairs to digest the proposals at leisure and report to his Government for instructions.

- 139. On the 28th October the American State Department presented to the Chinese Minister at Washington a similar draft treaty, a copy of which was handed by the American Minister to the Minister for Foreign Affairs at Nanking on the 9th November. Like the British proposals, the final American version had been slightly altered from the agreed draft of the 4th June, but, except for a few minor amendments and variations of form and the omission from the American draft of the reservation of other treaty port areas as well as Shanghai, the two sets of proposals were in the main identical.
- From the time of the presentation of the British proposals to the Minister for Foreign Affairs on the 11th September nothing was heard on the subject from the Chinese Government for some two months. On the 20th November, however, the Minister for Foreign Affairs reverted to the question with His Majesty's Minister, who was at that time again in Nanking. Dr. Wang said that he hoped to be able to present a formal Chinese counter-draft in a week or so's time, but meanwhile he desired to make a preliminary statement on the principal points in the British proposals which were unacceptable to the Chinese Government. The most important of these points were that the Chinese Government maintained its original desire to exercise complete jurisdiction immediately and was therefore unable to agree to the reservation of criminal jurisdiction; that the idea of foreign co-judges was not acceptable to the Chinese Government; that the Chinese Government was unable to agree to the nomination of the legal advisers by The Hague Court; that the Chinese Government could not agree to the principle of evocation; that if the reservation of the treaty ports were accepted the transfer of jurisdiction would be in name only; and that the Chinese Government would agree to the opening of the whole country to trade and residence only when all special privileges had been relinquished and relations between the two countries had been placed on a footing of perfect equality. Ten days later, on the 1st December, the Minister for Foreign Affairs presented the formal Chinese counter-proposals, from which, as forecast in his preliminary statement, there were omitted, as well as other important provisions of the British draft, the four major safeguards of reservation of criminal jurisdiction, foreign co-judges, rights of evocation and reservation of treaty ports. In fact, the new Chinese counter-proposals were little more than an elaboration of the original Chinese plan of January 1930, with the incorporation of some of the less contentious provisions of the British draft. His Majesty's Minister received these proposals without any special comment, informing Dr. Wang that he would send them home for consideration by His Majesty's Government and await the latter's instructions, which could not be expected to arrive for a couple of months or more.
- 141. On the 7th December the Chinese Minister in Washington submitted similar, but not identic, counter-proposals to the American Government.
- 142. Sir Miles Lampson returned to Peking early in December, and on the 17th December he received a telegraphic message from the Minister for Foreign Affairs expressing regret at the long delay in reaching a settlement, referring to the anxiety which was being caused to the minds of the Chinese people in connexion with their increasing desire for the immediate recovery of China's juridical sovereignty, mentioning the Chinese counter-proposals handed in on the 1st December, to which the Chinese Government were anxiously awaiting a favourable reply, expressing the earnest hope that a satisfactory solution of the question would be reached by the end of February 1931, and concluding with the veiled threat that the Chinese Government still believed it would be possible to settle the question by negotiation and that it would not be necessary for them to take a different course of action. To this message His Majesty's Minister, after consultation with the Foreign Office, sent a reply on the 27th December, referring to the fact that the Chinese counter-proposals had only been formally communicated to him on the 1st December, that they were now on their way home

to London for consideration by His Majesty's Government, and that His Majesty's Government did not, therefore, understand the necessity for such a message from the Minister for Foreign Affairs and hesitated to believe that the final sentence cloaked any intention of the part of the Chinese Government, by precipitate action, to prejudice the course of normal negotiations; His Majesty's Minister added that His Majesty's Principal Secretary of State for Foreign Affairs regarded it as most important to the prospects of a favourable conclusion to the negotiations that the atmosphere should not be embittered by threats on either side.

- 143. The same message was addressed by the Minister for Foreign Affairs to the American Government, and similar communications were also received by the French and Dutch Legations, except that, in their case, the Minister for Foreign Affairs, instead of referring to proposals already handed in, attached to his memorandum a set of proposals on the same lines as the counter-proposals he had already submitted to His Majesty's Government and to the American Government. The American, French and Dutch Governments all replied in due course on lines similar to the answer despatched by His Majesty's Minister.
- As indicated above, the American Government, after their one erratic and still unexplained step of the 23rd January, kept very much in line with His Majesty's Government throughout the year. Of the other Powers concerned, the French and the Dutch and the Norwegians adopted the general policy of waiting for a lead. As regards Japan, early in February the Japanese Government communicated to His Majesty's Government in the United Kingdom a statement of their attitude, namely, that they considered it inadvisable to proceed to an unconditional abolition of extra-territoriality, which would not only lead to confusion in China's relations with foreign countries, but would also entail equally harmful consequences to China herself; they had, however, already signified on more than one occasion their agreement, in principle, to the removal of the existing limitations upon China's jurisdictional freedom; and they were ready to propose to the Chinese Government a scheme for the progressive relinquishment of Japanese extra-territorial rights along the lines of the transfer, after the lapse of a stated period, of civil jurisdiction subject to safe-guards, including special courts and foreign co-judges, to be followed, after the lapse of a further stated experimental period, by the transfer of criminal jurisdiction, on the understanding that the whole country would be opened up to residence and trade for Japanese subjects, who would reciprocally enjoy all rights generally granted to foreigners in other countries, including rights in immovable property. The Japanese Government refrained, however, from making any definite move vis-à-vis the Chinese Government in the matter throughout the year, and declined to associate themselves with the proposals made by His Majesty's Government and the American Government, preferring apparently to wait and see what results might ensue from the British and American negotiations. Japan had, as a matter of fact, already successfully pursued this policy of procrastination for some time ever since her treaty had been denounced by China a few years before. She had at that time, while refusing to admit the Chinese contention, expressed her readiness to enter upon treaty revision negotiations, which she had managed to keep in the air ever since; so that, as Japanese extraterritorial rights had already in Chinese eyes lapsed (without any material change in the status of Japanese nationals in China), Japan's position was not, in theory, affected by the issue of the Chinese mandate of the 28th December,
- 145. The above account records the progress of the actual negotiations for the abolition, or rather modification, of extra-territorial rights during the year 1930. The position which existed at the beginning of the year following on the issue of the Chinese mandate of the 28th December, 1929, was naturally a delicate one, and it was a matter of satisfaction that so few dangerous incidents arose during the year, and that those which did occur were disposed of without the question of jurisdiction being forced to an issue. That serious trouble in this respect was avoided is probably to be ascribed in part to the preoccupation of the Chinese Central and local Governments with the civil war and in part to a genuine desire on the side of the Minister for Foreign Affairs to avoid serious trouble during the negotiations; while such incidents as did occur were firmly

and tactfully handled by His Majesty's consuls concerned. The most serious of these incidents was the affair of the arrest at Hankow of Paymaster Lieutenant-Commander McBride, R.N., on account of a motor car accident resulting in the death of a Chinese youth.

- 146. On leaving Peking in January to open the negotiations at Nanking, His Majesty's Minister had issued circular instructions to British consular officers in China explaining the position and summarising the correspondence between His Majesty's Government in the United Kingdom and the Chinese Government on the subject of the mandate of the 28th December, 1929. In this circular His Majesty's Minister concluded by stating that he was on his way to Nanking to initiate the negotiations, and that, in the meantime, the legal status of British subjects remained unaffected by the issue of the Chinese mandate; there was, however, a danger that some local authority might read the mandate as a licence to ride rough-shod over British extra-territorial rights; in any such case His Majesty's consuls should act as though the mandate had not been issued and refuse to admit its validity as affecting British subjects, concerting for that purpose, as and when necessary, with His Majesty's naval authorities where their assistance was available; at the same time His Majesty's consuls were to do their best to avoid incidents and to be careful not to back any provocative action on the part of British subjects, and generally to judge and deal with each case on its merits as it arose.
- 147. It was not long before an incident of the kind contemplated in these instructions occurred. On the 23rd January Paymaster Lieutenant-Commander McBride, while driving his motor car in the ex-German concession at Hankow, knocked down a Chinese boy, who died of his injuries an hour later.
- 148. Paymaster Lieutenant-Commander McBride was taken by the Chinese police to the local police station and detained there for some hours, until he was released as the result of the personal intervention of His Majesty's consul-general, who was obliged to give a letter undertaking that Paymaster Lieutenant-Commander McBride would not leave Hankow till the case was settled, and that he would be available to give evidence as a witness when required. From the outset of the case it was evident that the local police and judicial authorities at Hankow claimed jurisdiction over Paymaster Lieutenant-Commander McBride on the strength of the Chinese mandate of the 28th December, 1929, and while they had released him on what they professed to regard as a guarantee of his appearance in the Chinese courts when required, they had detained and obstinately refused to release his motor car.
- 149. His Majesty's Minister took the case up strongly at Nanking with the Minister for Foreign Affairs, who professed that instructions had been issued to all local authorities explaining the meaning of the Chinese mandate of the 28th December, 1929, namely, that, pending the result of the negotiations, British subjects, while theoretically under Chinese laws, were not in practice under Chinese jurisdiction. Whether such instructions, with their subtle explanation of what the mandate did and did not mean, had, in fact, ever been issued or not, it was quite apparent that the Chinese Government had gone as far as they dared, vis-a-vis their own people, in instructing them as to the real position of foreigners with extra-territorial rights, and that no amount of pressure would wring from the Chinese Government a statement in writing categorically instructing the Hankow authorities that British subjects were still under British jurisdiction and beyond the scope of the authority of the local Chinese courts.
- 150. In the meantime, the issue in the Hankow case had been narrowed down to the release of the motor car and the removal of the boy's corpse, which, more sinico, had been left lying on the spot. In spite of representations at Nanking and Hankow, the local procurator's office refused to return the car pending the completion of their investigations, and in due course they sent His Majesty's consul-general at Hankow a summons for transmission to Paymaster Lieutenant-Commander McBride to appear as defendant in a criminal case brought by the family of the deceased.
- 151. Eventually, however, the case, like so many other critical incidents in China, yielded to the passage of time and careful handling without any definite settlement being arrived at. The car was returned on the 5th March, and in

due course the boy's corpse disappeared from the scene of the accident. During March, April, May and June informal discussions proceeded, at first with the Chinese Government at Nanking and later with the local authorities at Hankow, regarding the payment of compassionate compensation to the family of the deceased, the figure of 300 dollars being mentioned on the British side and 5,000 dollars being demanded by the Chinese, who showed indications of readiness to settle for something over 1,000 dollars. Nothing definite, however, came of these negotiations, and on the 1st July Paymaster Lieutenant-Commander McBride left Hankow for Shanghai and England on transfer to another post. Before his departure the Minister for Foreign Affairs was informed in good time and warned that he was leaving, in order to prevent any possible charge of bad faith in connexion with the guarantee given by His Majesty's consul-general that he would appear to give evidence if required. No notice was, however, taken of this warning, and the case has since been allowed by both sides to lapse. On the whole the local Chinese authorities, though unwilling formally to renounce their claim to jurisdiction, showed no real desire to force the issue, and there was (probably on that account) comparatively little local agitation.

(2) Great Britain.

(a) General.

- 152. China's relations with the rest of the world have been undergoing a rapid change in recent years. The Kuomintang, which was established as the organ of a National Government in 1928, has from its inception made it a primary aim to place their country on a footing of equality in the community of nations; and the degree of success which they have already attained in this object has been one of their most striking achievements.
- 153. As early as 1926 His Majesty's Government in the United Kingdom indicated their sympathy with China's national aspirations in their December memorandum, and their recognition of the Nationalist Government in December 1928, foreshadowed as a national corollary an attempt at the readjustment of Sino-British relations. The task is a formidable one, in view of the extent and complexity of British vested interests in China, and the year 1929, which was spent largely in reconnoitring the position, produced little concrete progress. During the past year the two Governments have come to grips with the problem in earnest, and a good deal of successful work has been done. At the same time it has been possible to note a definite improvement in the tone of our relations with the Chinese Government, which has been generally satisfactory throughout the year.
- 154. The development of the extra-territorial question has been dealt with at length in the preceding section of the report. This issue, which has dominated the diplomatic horizon in China since 1929, still remains unsettled. The progress made may be summed up by recording that the year which had opened under the threat of the Chinese mandate of the 28th December, 1929, declaring extraterritoriality abolished, closed with the National Government committed to serious negotiations on a draft treaty for its gradual modification. The discussions on the subject were, moreover, conducted in a friendly atmosphere, which, contrary to our worst fears, was not disturbed by any serious attempt on the part of the Chinese authorities to infringe upon the treaty rights and liberties of British subjects.
- 155. Apart from this major issue, it may be said that the large proportion of outstanding questions which have been dealt with during the year have been brought to more or less satisfactory solutions, and much dead wood which had cumbered our relations with China in the past has thus been eliminated. Agreements were signed in the period under review for the rendition of Weihaiwei and the British Concession at Amoy, and for the return of the Boxer indemnity to China. The question of land tenure at Hankow, left in the air at the time of the rendition of the concession there, was finally regulated. Steps were taken to dispose of the Shakee, Wanhsien and Shanghai (the 30th May) incidents, which it is hoped will preclude any further raking up of these causes for agitation by the Chinese Government. In addition, the question of a Sino-Hong Kong Customs Agreement, which at the end of 1929, was threatening to become a

source of friction between the British Colony and China, seemed by the end of December on the way to an amicable settlement. (Please see in this respect the chapter on tariff and taxation.)

156. The conclusion of the international agreement for the rendition of the provisional court at Shanghai is described in the section dealing with the international Settlement.

157. The conduct of relations in China is still complicated by the situation of the National Government at Nanking. Accommodation in the new capital is almost as inadequate as ever, nor is the outlook sufficiently assured for any of the foreign Legations to have started or even seriously contemplated building operations on their own. Contact has been maintained with the Government, as in 1929, by periodical visits on the part of His Majesty's Minister, who has been represented in the intervals by a member of his staff (since March 1930, Mr. E. M. B. Ingram, counsellor of His Majesty's Legation), spending his time as circumstances indicated either in Shanghai or Nanking. Permanent offices adjoining His Majesty's consulate-general in Nanking have, however, been acquired for the Legation, as well as makeshift accommodation for the staff of the Minister during his visits. Sir Miles Lampson himself spent some ten weeks in Nanking in the course of four tours, during which he was away from Peking for 136 days in all.

158. On the 3rd January His Majesty's Minister left Peking in order to initiate the dicussions regarding extra-territoriality, to which His Majesty's Government in the United Kingdom were committed by their memorandum of the 20th December. As was expected, the opening moves of the negotiations on this subject did not lead very far. Both sides defined their positions and drew back for further consideration. But, having set the negotiations on foot, His Majesty's Minister was able to obtain from the Minister for Foreign Affairs assurances that precautions would be taken to avoid incidents resulting from the Chinese Government's mandate of the 28th December, which might have been interpreted as meaning that British subjects were liable to arrest by the Chinese authorities. (The only incident of this kind arising during the year which offered serious difficulty was the arrest at Hankow of Paymaster Lieutenant-Commander McBride, see above, section 151.)

159. Throughout this visit negotiations were going on between the delegates of the foreign Legations and China for the rendition of the Shanghai Provisional Court, and the intervention of His Majesty's Minister was instrumental in securing agreement in the matter before his return to Peking at the end of February. Most satisfactory progress was also made with the negotiations for the rendition of Weihaiwei and the return of the Boxer indemnity on both of which subjects draft agreements were completed and initialled for reference to the respective Governments.

160. In order, if possible, to conclude these two agreements, Sir Miles Lampson again visited Nanking in April. It was not possible actually to go further with the discussions on the Boxer indemnity owing to the absence of instructions from London, but agreements were signed covering the rendition of Weihaiwei. At the same time, on the initiative of His Majesty's Minister, negotiations were set in train with a view to handing back the comparatively valueless concession at Amoy in accordance with the policy of His Majesty's Government to divest themselves progressively of commitments in China as far as it can be done with due regard to British vested interests.

161. No attempt was made at this time to continue the discussions on extra-territoriality, with regard to which His Majesty's Government were still considering the terms of concrete proposals to be made to the Chinese Government. Sir Miles Lampson informed Dr. Wang that he did not expect to be able to hand these proposals to him before September, and the latter did not demur at the necessary delay. The Chinese Government, indeed, evidently appreciated the readiness of His Majesty's Government, evinced during this visit, to continue steadily their policy of reasoned concession to Chinese aspirations, in spite of the weakened position of the National Government, whose authority was being seriously challenged by Marshals Yen Hsi-shan and Feng Yu-hsiang in the North. The Northern rebellion continued throughout the

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summer and led incidentally to some friction with the National Government over the position of Mr. B. Lennox-Simpson, a British subject, whose services had been enlisted by Marshal Yen, first as a journalist to conduct press propaganda, and later to take charge of the maritime customs at Tientsin, which had been taken over by the Northern allies. Repeated attempts were made by the Government at Nanking to induce the British authorities to take legal action against Mr. Simpson for engaging in activities hostile to the recognised Government of China. The refusal of His Majesty's Government to sanction this, both on grounds of law and equity, caused a degree of bitterness at Nanking, which was probably due to constitutional inability to appreciate a policy of strict neutrality and a consequent uneasiness lest this should mean that we were disposing ourselves to play off one side in the civil war against the other.

- It was partly in order to combat such suspicions that His Majesty's Minister decided to visit Nanking again in September in order to continue the extra-territoriality negotiations as he had promised, in spite of the precarious situation of the National Government. In addition, the exchange of ratifications of the Weihaiwei agreements, on which the date of the rendition of the territory was dependent, was due to take place on or before the 1st October, and it was considered undesirable to prejudice the agreements by withholding rendition if the state of the country made it in any way possible to proceed. The policy of His Majesty's Government in this respect was eventually fully justified. The British draft treaty on extra-territorial jurisdiction was handed to Dr. Wang on the 11th September. The rendition of Weihaiwei took place as arranged on the 1st October. In addition, notes embodying agreed terms for the return of the Boxer indemnity to China were exchanged by Sir Miles Lampson and Dr. Wang. The Northern rebellion collapsed at the end of September; and the Lennox-Simpson case received a melancholy solution in the assassination of Mr. Simpson at Tientsin on the 1st October by unknown Chinese assailants. The Nanking Government duly expressed regrets at the event, but the measures which they promised for the arrest of the assassins remained ineffective, as, indeed, they might well do in the prevailing disturbance, however seriously they were prosecuted.
- 163. The success of the National Government in the civil war was hailed in Nanking with a series of celebrations, and a visit of courtesy was paid to the capital in November by His Majesty's Minister and other foreign representatives who had been invited to attend.
- 164. Sir Miles Lampson prolonged his visit in order to be able to introduce to the Chinese Government the British Economic Mission to the Far East, which arrived in Nanking at the beginning of December (please see the chapter on trade).
- 165. Minor questions continued, in the present unsatisfactory state of affairs in China, to irritate the surface of our relations with her, in particular the failure of the Chinese Government to pay its debts to British subjects and the danger to British life resulting from disturbed conditions in the interior.
- the Chinese Government as occasion arose to redeem their various outstanding obligations towards British interests, calling attention to defaults in the service of railway loans and failure to pay debts for material and the salaries of employees, but with scant success. After some difficulty, His Majesty's Minister obtained from the Minister for Foreign Affairs in May an undertaking to pay off by monthly instalments the amount assessed as compensation to the sufferers in the Nanking incident of 1927, towards which only the initial payment of 300,000 dollars, as against a total of roughly $2\frac{1}{2}$ million dollars, had by them been made. Up till the end of the year, however, only a further 100,000 dollars was received out of the 1,300,000 dollars which should have been paid under this arrangement. The calling of a conference by the Chinese Government in November to consider the consolidation of their unsecured debts is described in the financial chapter of the report.
- 167. In May, following a suggestion made by the Chinese authorities, British subjects were advised to evacuate the interior of Hupeh, Kiangsi and

Hunan, south of the Yellow River, and His Majesty's consuls elsewhere have since been instructed to lose no time in advising similar withdrawal should they think it desirable, in view of the serious spread of communism and banditry in Central China. In spite of these precautions, there have been no fewer than fourteen cases of attacks on British subjects, of whom five were murdered by bandits during the year. Eight British missionaries were carried off and held to ransom in the interior. The most distressing case was that of Miss Nettleton and Miss Harrison, of the Church Missionary Society, who were captured by Communists in North Fukien in June, and finally were brutally done to death after prolonged efforts to secure their release. The undertakings obtained from the Central Government to bring the murderers to justice have remained unfulfilled owing to their lack of control in the neighbourhood.

- 168. Active anti-foreignism appears, on the other hand, to have died down. The only serious anti-British agitation to be recorded arose out of labour trouble at the factory of the International Export Company at Nanking, in connexion with which a hostile demonstration was held outside His Majesty's consulategeneral just before Sir Miles Lampson's visit in April. A sharp reminder from His Majesty's Minister brought the Chinese Government to a realisation of their responsibilities, and a recurrence of the trouble was energetically repressed.
- 169. The treatment of Sir Aurel Stein's Central Asian expedition indicates, however, how the anti-foreign complex lingers in the minds of the Chinese leaders. Sir Aurel visited Nanking in April, and, having explained his objects fully to members of the Government, obtained, through the good offices of His Majesty's Minister, a passport entitling him to travel in Sinkiang for the purpose of studying ancient remains. Subsequently, owing to the jealousy and suspicion of the National Commission for the Preservation of Antiquities (a sub-department of the Chinese Government), persistent obstructions have been placed in the way of his work in Sinkiang which render the success of his expedition doubtful.
- 170. Taxation and land cases (of which the most serious was one concerning a waterfront property at Shanghai owned by Messrs. Butterfield and Swire) have been less acute during the year, with a growing realisation that, in view of the probable modification of the extra-territorial system, it is more important for British firms to cultivate good relations with the Chinese authorities than to maintain their strict rights under the treaties.

(b) Weihaiwei.

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171. The negotiations for the rendition of Weihaiwei were reopened in January, when His Majesty's Minister communicated to the Chinese Minister for Foreign Affairs the reply of His Majesty's Government in the United Kingdom to the proposals submitted by Dr. Wang the previous June. These proposals constituted an attempt by the Chinese to recede from the terms agreed upon in the draft convention of 1924 and to curtail considerably the concessions to be made to Great Britain. Dr. Wang was evidently impressed by the firmness of the British reply, which Sir Miles Lampson had for some months been awaiting an opportunity to deliver, and of the nature of which he must already have been informed by the Chinese Minister in London (please see China annual report for 1929). In any case, he adopted a much more yielding attitude. In June 1929 he had stated that the Chinese Government desired to make Weihaiwei a naval base, on which pretext his proposals had indicated the intention of closing the territory to foreign residence and trade and limiting drastically the facilities to be accorded there to His Majesty's navy after rendition. The reply of His Majesty's Government on the first point was reasonable and conclusive. They maintained no objection to the reservation by the Chinese Government of the right to close the territory (although Sir Miles Lampson pointed out that this must be regarded as an unnecessary and retrograde step), but pointed out that, in the event of their doing so, foreign property owners would, in the event of exclusion, have to receive fair compensation. This provision, to which the Chinese could take no exception and which was eventually embodied in the

Rendition Convention, makes it exceedingly unlikely that they will find it worth their while to exercise the right for which they have stipulated. In other respects Dr. Wang early indicated his readiness to abandon his June proposals and return to the basis of the 1924 draft, and it soon became evident that the negotiations were to turn almost entirely on the question of the period for which the facilities to be allowed to the British navy at Weihaiwei after rendition should be continued. Article 23 of the 1924 draft provided that the Chinese Government should loan to His Majesty's Government for the use of the navy a certain number of buildings and facilities on Liukungtao "for a period of ten years with the option of renewal on the same terms by agreement between the two Governments." An attached exchange of notes was to record the understanding that renewal would not be refused "without reasonable cause" and that any disagreement should be referred to arbitration.

- To the list of facilities drawn up in 1924 Dr. Wang in his more tractable mood took no exception, and he abandoned early in the negotiations his original opposition to the initial term of ten years. He remained firmly opposed to any option of renewal thereafter. Subsequently, at his request, the matter of the 1924 draft was divided and two new drafts drawn up, of which the first contained the "civil" clauses of the 1924 text in a revised and shortened form and the second the whole of the naval clauses. These two documents Dr. Wang declared himself ready to sign, but without the exchange of notes on the subject of renewal of the loan of facilities. Eventually he was induced to agree to the alteration of the words governing the period of the loan to read "with the option of renewal on the same terms or on such other terms as may be agreed upon.' The two drafts were then adopted and initialled ad referendum to the respective Governments on the 14th February. They represented terms considerably more favourable than might have been expected from a Nationalist Government, and Sir Miles Lampson therefore recommended their acceptance. The drafts, with some minor amendments, duly received the approval of His Majesty's Government, and the two instruments, the Convention for the Rendition of Weihaiwei and the agreement regarding facilities for His Majesty's navy, were signed at Nanking on the 18th April. In order to permit of the continued use of the military convalescent depot at Weihaiwei during the following summer, it was provided that the convention should come into force upon the exchange of ratifications, which was to take place on or before the 1st October, and at the time of signature His Majesty's Minister addressed a letter to the Minister for Foreign Affairs informing him that His Majesty's Government would not feel bound to carry out rendition if, when the time for it came, the Chinese Government were not in control of Shantung.
- 173. That this was not an idle consideration was shown in the course of the summer, during which Tsinan was captured by the Northern opponents of the Central Government, and it became a moot point whether or not it would be possible or advisable to hand over Weihaiwei to the Nanking authorities. Sir Miles Lampson recommended that if possible nothing should be allowed to stand in the way of rendition unless the Central Government themselves requested postponement, and he was accordingly instructed in September to ask the Minister for Foreign Affairs for a statement indicating the ability of his Government to maintain order in Weihaiwei. A satisfactory declaration having been obtained, it was decided to proceed, and the ratifications of the convention and agreement were duly exchanged on the 1st October, on which date the territory of Weihaiwei was formally handed back to China.
- 174. The Chinese Government had informed His Majesty's Government of their intention to constitute the territory a special district to be administered directly under the Executive Yuan by a High Commissioner; Captain Hsu Tsu-shan was appointed to this post and arrived in Weihaiwei on the morning of the 1st October with Mr. Wang Chia-cheng, Vice-Minister for Foreign Affairs, as Chinese delegates to take over the territory. With the co-operation of the British naval authorities the transfer was carried out in a ceremonial manner, following the precedent of the handing over of Heligoland to Germany. The Commander-in-chief, Sir A. K. Waistell, attended the ceremony in person. The inauguration of the new Chinese Administration, in the course of which tributes were paid to the beneficence of the past British rule, was conducted in an orderly

and friendly atmosphere. The British Commissioner, Sir R. F. Johnston, left in H.M.S. "Sandwich" in the afternoon, and the British garrison were withdrawn the following day. The Chinese authorities took over the existing local police force, and a force of marines was landed to keep order in the territory. The district officer, Mr. Archer, remained (with some of the other British officials) to assist the Chinese Administration in taking over, having been appointed acting British consul at Weihaiwei.

175. Under the terms of the convention all Government land, buildings, stores and other property were handed over free of charge to the Chinese Government, with the exception of those reserved for the use of His Majesty's navy and of certain properties leased to His Majesty's Government for the use of His Majesty's consulate and the foreign residents. The British title deeds to land held by foreigners were subsequently exchanged, as provided in the convention, for Chinese deeds of perpetual lease. It is laid down that, if the Chinese Government decide to close the territory to foreign residence, a Sino-British commission will be appointed to assess the compensation to be paid to foreign property owners and leaseholders.

176. Up to date the new Chinese administration appears to be functioning smoothly and efficiently.

In general, the conclusion of the rendition negotiations can be regarded as highly satisfactory. His Majesty's Government committed themselves at the Washington Conference to the return of Weihaiwei to China subject to the retention of facilities for the use of the port as a summer sanatorium by the China Squadron, which represented the main practical value of the territory to Great Britain. The Naval Facilities Agreement as eventually signed gives no real security for the continuance of these facilities for more than ten years; but, in view of the trend of events in China since 1922, to have obtained the ten-year period was itself a success hardly to be hoped for, and one which we should have been more and more unlikely to secure the longer the conclusion of the negotiations was postponed. Apart from this, the terms of the convention and agreement are in some minor points even more favourable than those of the 1924 draft. The return of the territory is one more step in the readjustment of Sino-British relations and as a generous gesture, which appears to have been not unappreciated by the Chinese, should contribute to improvement of our position in China, where any further delay in implementing our promises in this respect would have had the contrary effect.

(c) The Boxer Indemnity.

178. An agreement was reached during the year for the return to China of the British share of the China indemnity of 1901. The terms embodied in the agreement were based upon the decision reached by His Majesty's Government in the United Kingdom in 1929 to hand over the indemnity funds to the control of the Chinese Government on the understanding that they should be applied in general conformity with the recommendations of the Indemnity Advisory Committee appointed in 1925, and subject to a proviso that all orders for materials purchased abroad out of the funds should be placed in the United Kingdom. Proposals to this effect had been made to the Chinese Government during the previous year, and had been welcomed by them. Certain amendments to the text of the proposals put forward on the Chinese side, coupled with outside indications that they proposed to use the greater part of the funds for the completion of the Canton—Hankow Railway, had, however, caused His Majesty's Government to become concerned over the possibility of a conflict between their obligations under the Consortium Agreement of 1922 and the stipulation with regard to the purchase of materials in Great Britain. At the end of the year a modified scheme was being worked out to guard against this possibility.

179. The new proposals which were embodied in a draft exchange of notes reached His Majesty's Legation in December 1929, and were submitted to the Minister for Foreign Affairs by His Majesty's Minister in January. The main alterations introduced consisted in a proposal that the Chinese Government should appoint a Purchasing Commission in London to which the bulk of the funds would be handed over to be expended in the United Kingdom on materials

required by the Chinese Government for the productive works in which it was their intention to invest the money. This proviso, while it tightened up considerably the original stipulation with regard to the placing of orders in Great Britain, removed any possibility of contioversy arising in connexion with the funds over the various obligations of the parties regarding open tender, since it made it clear that any materials purchased out of the indemnity would be, in effect, a gift from Great Britain to the Chinese Government.

- 180. The new texts were eventually agreed to by Dr. Wang with minor amendments and initialled for reference to His Majesty's Government on the 19th February. Some months were spent in the consideration of the Chinese amendments, and in a slight readaptation of the form of the agreement which was considered desirable in order to bring it into line with the terms of the Bill that was being drafted to give effect to the proposals. And the agreement was finally concluded between Sir Miles and Dr. Wang in September. It took the form of a series of notes signed on two different dates, in the first of which, dated the 19th September, Dr. Wang put forward a proposal for the return of the indemnity funds to China, and stated the manner in which they would be applied if so returned: Sir Miles Lampson acknowledged Dr. Wang's proposals and stated that they were being referred to His Majesty's Government. In a further note dated the 22nd September, Sir Miles Lampson informed Dr. Wang that His Majesty's Government approved the proposals and would remit the funds accumulated since 1922 and all future payments on the conditions proposed, subject to the necessary legislation being passed in Parliament.
- 181. The arrangements laid down for the disposal of the land with the laws. The Chinese Government expressed the intention of dealing with the land with the report of the Indemnity The arrangements laid down for the disposal of the funds were as money in general harmony with the views set out in the report of the Indemnity Advisory Committee. They proposed, however, in the first instance to devote the bulk of the funds to the creation of an endowment for educational purposes by investing them in railway rehabilitation and construction and other productive enterprises. The accumulated funds, together with a half of all future instalments, are to be handed over to the London Purchasing Commission for expenditure on material in the United Kingdom. The remaining half of the future instalments is to be paid to a board of trustees (to include British members) which will be set up by the Chinese Government to administer the endowment. funds spent in the United Kingdom will be regarded as loans from the board of trustees to the Chinese Government, the interest and amortisation of which will be applied to the purposes of the endowment. The Purchasing Commission is to be composed of the Chinese Minister in Lendon, a representative of the Chinese Ministry of Railways, and four other persons appointed by the Chinese Government from a panel of persons recommended by His Majesty's Principal Secretary of State for Foreign Affairs. A separate exchange of notes provides for two grants for educational purposes out of the accumulated funds, one to the Hong Kong University of £265,000, and one to the Universities' China Committee of £200,000. In addition it was agreed in an unpublished exchange of letters that the Chinese Government would recommend to the board of trustees a grant of £20,000 to the British Charitable Hospital in Peking, and one of £40,000 for the construction of a new Waichiaopu building at Nanking. Finally, in unpublished notes exchanged at the time of the conclusion of the agreement, the Chinese Government's intention is recorded, in connexion with their programme of railway rehabilitation, to arrange for the early settlement of outstanding debts for railway material supplied by British subjects. This was the utmost that His Majesty's Government felt they could do towards using the return of the indemnity as a lever for assisting the unfortunate British creditors in question, consistently with their policy of adhering to the principles laid down in the Advisory Committee's Report, and not diverting the indemnity funds to the settlement of British claims against the Chinese Government.
- 182. The original suggestion entertained in 1928, that His Majesty's Government should remit the indemity to the unfettered control of the Chinese Government, had undergone substantial qualification in various directions by the time the final agreement was drawn up. This was due to the growing urgency of assisting British industry, to the considerations connected with our consortium obligations, and to an increasing conviction on the part of His Majesty's Minister

(based on the experience of the United States Legation) that to omit altogether some safeguard against the misappropriation of the funds would be an act of unjustifiable irresponsibility towards the interests both of the British taxpayer and the Chinese people; for this reason the control of future payments to the Purchasing Commission and the Board of Trustees was retained in the hands of His Majesty's Legation. The agreement has been criticised on the one hand on the ground that charity should begin at home, and that it is quixotic to hand over large sums of money to a Government which declines to pay its debts to British subjects; and on the other as an unavowed abandonment of our previous generous professions, since it is alleged that, in order to secure the benefit of the funds for British industry, we have sacrificed the claims of the educational and similar objects to which the Advisory Committee's report attached primary importance. Certainly, the implication that the main object of the arrangement laid down is the establishment of an endowment for educational purposes is to some degree fictitious, and it remains to be seen whether any considerable sums will be made available for these purposes. It is, however, a plain fact that the most immediate need of China at the moment is material reconstruction (just as our own most pressing requirement is employment for our industries) and the expenditure of the indemnity funds on the improvement of railway communications is undoubtedly the most practical way of using them for that object, and one which, though it may not bring us in as rich a harvest of favourable publicity as the creation of a generation of British-returned students, will almost certainly be far more beneficial to China.

183. The China Indemnity (Application) Bill, drawn to give effect to the terms of the agreement, was introduced into Parliament on the 12th December.

(d) Revival of the Wanhsien and Shakee Incidents.

Minister for Foreign Affairs reopened the questions, which for some time had seemed forgotten, of the Shakee "massacre" of June 1925, and the bombardment of Wanhsien in September 1926; and on the 1st May he presented a memorandum requesting that discussions should be opened with a view to their settlement. This step was probably forced upon him by the hotheads of the Government, and was one which it seemed important to counter before an agreement was entered into for the return of the Boxer indemnity. This was successfully done by Sir Miles Lampson, who pointed out at once to Dr. Wang the inappropriateness of raising this question at a time when His Majesty's Government in the United Kingdom were proposing to remit to China the considerable indemnity to which they were fully entitled, and assured him that Parliament was most unlikely to vote any money to China for the settlement of the incidents in question if remission of the Boxer funds had been previously agreed to. He suggested tentatively, as the only possible solution which occurred to him, that a grant might eventually be made by the Chinese Government to the sufferers in the two incidents out of those funds. He made it plain that, in any case, Dr. Wang's inopportune action might seriously delay a settlement of the indemnity question.

185. His Majesty's Government were, it turned out, unwilling definitely to connect this question with that of the indemnity, or to make the conclusion of the indemnity agreement dependent on the withdrawal of the Chinese claims in respect of the incidents. His Majesty's Minister was, however, able, at the time of the signature of the indemnity notes, by intimating that any outstanding claim for compensation by the Chinese Government might effect the attitude of Parliament to the agreement, to obtain from Dr. Wang a letter in which he withdrew his memorandum of the 1st May, and undertook that he personally, as Minister for Foreign Affairs, would not reopen the question.

(e) The Kuomintang in Malaya.

186. The question of the Kuomintang organisation among the Chinese in British Malaya has threatened to become a serious issue in Sino-British relations. The Kuomintang had been regarded as a dangerous body by the Malayan

authorities since the reorganisation of the party under the influence of the Communist movement in 1924, and the position of the local branches had long been anomalous. Under the Societies Ordinances of the Malayan Governments any society unregistered with the local authorities is deemed to be illegal, and registration had been consistently refused to the Kuomintang on the ground that its activities were prejudicial to peace and good order. A general branches in Singapore and local branches and sub-branches throughout the Colony and Protectorates were known nevertheless to exist and to function more or less secretly, and their activities, some of which were of an undesirable nature, were closely watched by the authorities.

- 187. After the recognition of the Kuomintang Government in China by His Majesty's Government, the question of removing the ban on the party organisation in Malaya came under discussion. The local Governments were unwilling to accord the society official recognition, on the ground that to do so would enable it, by using indirect pressure, rapidly to extend its organisation among the non-politically-minded Chinese population to a degree which would render it a serious danger to government. Instances were given of the dissemination by the society of subversive propaganda based on the anti-imperialist doctrines of the tang, but what was chiefly feared was the existence per se of a powerful organisation controlled from abroad among a racial group comprising more than half the total population.
- 188. His Majesty's Minister, on the other hand, on being asked for his views, took the line that to proscribe the Kuomintang in Malaya as such, while in friendly relations with the National Government, was illogical and put us definitely in the wrong; whereas, if we recognised the society, we should at once strengthen our position for dealing drastically with any disloyal or subversive activities on the part of individuals or branches, and, if necessary, protesting to the Chinese Government.
- 189. The question came up at a meeting of the Secretaries for Chinese Affairs of Hong Kong and Malaya, which was held at Hong Kong in November 1929, and was attended by His Majesty's consul-general at Canton, representing His Majesty's Legation. Mr. Moss explained to the meeting the views of His Majesty's Minister The Malayan representatives were unwilling to recede from their attitude with regard to the organisation of the tang in Malaya. At the suggestion of Sir Cecil Clementi, the Governor of Hong Kong, who was proceeding shortly to take up his new appointment in Malaya, further consideration of the problem was suspended pending his arrival in Singapore.
- 190. Sir Cecil Clementi reached Singapore on the 5th February, on which very date a conference was being held of the Malayan General Branch of the Kuomintang. This conference, which was conducted more openly than previous meetings, was regarded as a challenge to the authority of the Government and, on the advice of his experts, Sir Cecil Clementi decided that the ban which already existed against the tang organisation, should be immediately made effective, and on the 20th February he ordered the dissolution of the Singapore General Branch and the branches throughout Malaya.
- 191. This step was carried out without opposition from the local Chinese population and proved satisfactory from the point of view of the Malayan Government in curbing the activities of the tang. On the 24th February the Chinese Chargé d'Affaires in London raised the question with the Foreign Office, and requested that steps be taken to reverse the policy of the Malayan Government. After inter-departmental discussions it was proposed to reply to the Chinese Chargé d'Affaires, pointing out that the closing of the tang branches was not a reversal of policy on the part of Malayan authorities since their existence was already illegal, and explaining that the Kuomintang could not be allowed in Malaya unless its aims were compatible with complete loyalty to the local Government. His Majesty's Minister, while expressing the opinion that a more effective reply would be to carry the war into the enemy's country by enquiring whether the Chinese Government did in fact approve of the activities indulged in by the

Kuomintang in Malaya, suggested that, as a long delay had intervened, the question might be allowed to lapse in view particularly of the precarious situation of the Government in China. It was, indeed, no doubt only due to the preoccupation of Nanking with the Northern rebellion that the repercussions of the affair on our relations in China were not more immediate and violent. During the summer the issue slumbered. The Malayan branches functioned, if at all, only underground, though a certain amount of propaganda continued to be received from China. On the 28th July, however, two Chinese, Chen Lo-sheng and Fan Chih-chen, were banished from Malaya in connexion with the discovery of certain circulars issued over their signatures and purporting to emanate from the Malayan General Branch of the Kuomintang. This concrete indication of the Malayan Government's intention to enforce the ban with a firm hand gave rise to an agitation in the China press. Mr. Hu Han-min attacked the British authorities in a series of violent articles and speeches. And at the end of H_Is Majesty's Minister's visit to Nanking in September, Dr. Wang took up with him personally the case of these two men (into which Sir Miles Lampson promised to enquire), and then handed in a memorandum in which he raised not only this case but the general issue of the suppression of the Malayan branches. Sir Miles Lampson had previously staved off any attempt on the part of the Minister for Foreign Affairs or others to press this question, by expressing very strong views as to the behaviour of the Kuomintang in British territory, their dissemination of subversive propaganda, attempts to carry out registration of Chinese schools, introduction of anti-imperialist text-books and the like. In the circumstances, it was decided to continue to ignore for the time being the general aspect of the question as raised in Dr. Wang's memorandum. Sir Miles Lampson was at that time thinking of paying an unofficial visit to Singapore at the beginning of 1931, and it seemed desirable that the occasion should be used for a full consultation with the Colonial authorities on the subject. Accordingly, on visiting Nanking again in November, His Majesty's Minister informed the members of the Chinese Government unofficially of his proposed visit, and expressed the hope that he would be better able to discuss the question of the tang in Malaya with a view to a settlement after studying the problem with the British authorities on the spot. This enabled the issue to be postponed, and the Chinese agitation appeared to have died down by the end of the year, when Sir Miles Lampson left for Singapore.

(f) A moy.

192. The status of the British concession at Amoy, the oldest British concession in China, has always been unsatisfactory. Our title has rested on an exchange of notes between His Majesty's consul and the Chinese Taotai, dated the 9th February, 1852, by which the land occupied by the concession was granted "to the English merchants to build godowns thereon." The area has, in any case, long been of negligible importance for commercial or residential purposes, being practically indistinguishable from its surroundings.

193. In February His Majesty's consul at Amoy submitted a proposal that the concession should be rendited on the lines followed in the case of the British concession at Chinkiang. Sir Miles Lampson had himself had this matter in mind, and was awaiting a suitable moment to broach it with the Minister for Foreign Affairs. This occurred on the 21st April, when the question of the exchange of Crown leases at Hankow and Kiukiang was also raised. Dr. Wang agreed to Sir Miles Lampson's suggestion that the matter should be dealt with by an exchange of notes cancelling the head lease from the Chinese Government to His Majesty's Government, and providing for the exchange of Crown leases for Chinese deeds of perpetual lease. On the 30th May, draft exchanges of notes were transmitted to the Waichiaopu on the lines of the Chinkiang precedent, but with minor alterations to cover the differences in the status of the two concessions. Counter-drafts were in due course exchanged, but no vital amendments were necessary and the notes were finally signed and exchanged on the 17th September.

194. The main notes provided for the issue of Chinese deeds of perpetual lease to the lot-holders and simultaneous cancellation of the notes of 1852. Thus

the rendition of the concession was to take effect from the date on which the Chinese deeds were issued to foreign lot-holders. The subsidiary notes merely contained an assurance regarding the maintenance of the land tax at the existing rate pending the actual application throughout the Amoy district of the new law governing land taxation throughout China. It is perhaps worthy of remark that the Chinese refused to admit a clause in their first note to express gratitude for the return of the concession as had been done in the case of Chinkiang. Dr. Wang stated that he would prefer to express thanks when the rendition had been completed, but in fact he has not yet done so.

195. All the complicated details in connexion with the exchange of Crown leases for Chinese title deeds were dealt with locally at Amoy, as well as questions relating to the winding up of municipal affairs. Since the disbandment of the Concession Police Force in 1925 and their replacement by police controlled by the Chinese City Commissioner of Police, the functions of the municipal council of the concession have been negligible. No rates or taxes have been collected for the past five years, and such minor expenses as have arisen had been met out of surplus funds in hand. At a final meeting of the ratepayers of the concession called by His Majesty's consul on the 8th November the council's affairs were wound up, and it was decided to utilise the balance of the funds, first to pay the expenses incurred in connexion with rendition and then to hand over the residue of some 1,800 dollars to the Chinese Commissioner of Police as a voluntary contribution for their services in the concession since 1925. This was done in due course.

196. On the 30th December Mr. Grant Jones received from the Amoy magistrate the duly executed Chinese deed of perpetual lease for lot-holders other than Chinese, and on that date therefore the Amoy British Concession ceased to exist.

(g) Hankow and Kiukiang Crown Leases.

The Chen-O'Malley Agreement of 1927 relating to the rendition to China of the British concessions at Hankow and Kiukiang dealt only with the administration of those areas and left in the air the question of land tenure. The local Chinese authorities at Hankow have, however, during the past three years, attempted to argue that the agreement also had the effect of abrogating the title of His Majesty's Government to the ownership of land in the ex-concession and its extension under the existing head leases. The principle of the exchange of Chinese deeds of perpetual lease for British Crown leases having been established in the Chinkiang rendition exchange of notes and confirmed at Weihaiwei, the time seemed ripe to attempt a settlement of this Hankow and Kiukiang land tenure question. Accordingly on the 21st April His Majesty's Minister raised the matter with the Minister for Foreign Affairs, and the latter without demur expressed his willingness to proceed with a settlement on the same lines as at Chinkiang. The Waichiaopu were, however, unable to get the necessary archives from Peking owing to the occupation of the former Waichiaopu by Yen Hsi-shan's adherents, and it was not until December that Dr. Wang was able to deal with the draft notes which had been handed to him in April. It was then found that the Waichiaopu were unwilling to admit any reference in the notes to the existence of the 1861 and 1898 Lease Agreements (covering the Hankow concession and its extension respectively). They feared local criticism which would be based as shown above on the ground that these lease agreements had been abrogated under the 1927 Hankow Agreement. Eventually it was decided, by way of saving Chinese "face," to proceed straight away with the exchange of Crown leases for Chinese deeds of perpetual lease, and afterwards to effect an exchange of notes stating that in view of the Rendition Agreement of 1927 and the subsequent issue of Chinese deeds, the old agreements of 1861 and 1898 were abrogated. Local negotiations were accordingly entered upon between His Majesty's consul-general and the Chinese Director of the Municipal Bureau in order to put this arrangement into effect.

(3) Canada.

198. The Hon. Herbert Marler, His Majesty's Minister for Canada in Japan, accompanied by members of his staff, paid two visits to China in the course of the year. The party arrived in Shanghai on their first visit on the 13th March, and proceeded on the 18th March to Nanking, where Mr. Marler conferred with prominent members of the Chinese Government on the question of extending Canadian trade in China, returning to Japan from Shanghai on the 22nd March.

199. In September Mr. Marler visited North China, reaching Mukden on the 18th September, where he was entertained by Marshal Chang Hsueh-liang. Owing to disruption of railway traffic, he did not arrive in Peking until the 25th September. He and his party were entertained in my absence by the members of His Majesty's Legation. Mr. Marler afterwards attended at Tientsin a luncheon given in his honour by the British Chamber of Commerce, and on the 29th September returned to Japan.

200. A Canadian trade delegation to the Far East, organised by the Canadian Chamber of Commerce, visited Shanghai from the 16th to the 18th November. The delegation was originally intended to remain in Shanghai for a number of days, which would be devoted to a serious examination of the possibilities of increasing Sino-Canadian trade. Unforeseen circumstances, however, compelled them to hasten their departure, and this visit was actually little more than a preliminary gesture of friendship and interest. The possibility was mentioned of a second visit during which the trade question would be closely and thoroughly examined.

(4) Japan.

201. In 1929 Japan, finding her isolated forward position among the Powers untenable, and under the influence of economic pressure, changed her "positive policy" in China to a "policy of adaptation." During the past year she may almost be said to have developed this into a policy of self-effacement. Setting aside the part played by Japan with regard to the summoning of the Debt Conference at the end of the year, neither in Manchuria nor in China proper has she allowed herself to come to the fore with any salient move, and on the contrary, where matters of common interest were concerned, has shown a tendency to keep in shelter behind the other Powers. This access of retiringness is no doubt the result of extreme financial and industrial depression. In the future Japan will inevitably play a leading part once more in Sino-foreign diplomacy, but for the moment the supreme importance to her of the Chinese market has an opposite effect, and her immediate concern is to avoid provoking any further explosion of the acute hostility which her encroachments of former years have engrained in the mind of Nationalist China.

202. In conformity with their new policy, the Japanese Government have allowed the question of the appointment of a Minister to China to remain in abeyance. In January 1930 Mr. Shigemitsu, consul-general at Shanghai, was appointed concurrently Chargé d'Affaires. This has served the double purpose of imposing naturally on the Japanese representative a retiring rôle and of enabling the Japanese Government to keep in close touch with Nanking without ostensibly breaking away from the rest of the Powers by transferring their

Legation to the south.

As described elsewhere, Japan played no part in the discussions on the subject of extra-territoriality or in the negotiations for the revision of the Shanghai Provisional Court. The Japanese Legation was kept fully informed by His Majesty's Minister at every stage of the progress of these negotiations, and an attempt was made to induce the Japanese Government to join His Majesty's Government and the United States in the presentation to China of the agreed proposals embodied in the British extra-territoriality draft of the 11th September. The former declined, however, to commit themselves on the pretext that they had not had time to consider the terms of the draft, and have throughout the year successfully maintained an attitude of watchful aloofness towards the British and American negotiations in which the Chinese Government have acquiesced,

no doubt considering that they are far more like'y to obtain a favourable agreement from Great Britain or the United States, after which they will be in a strong position to impose similar terms on Japan.

- 203. As regards the Shanghai Court Agreement, the Japanese authorities have acquiesced in the functioning of the new courts without formally adhering to the agreement.
- 204. Early in the year the Minister for Foreign Affairs began to press Mr. Shigemitsu on the subject of treaty revision, and proposed the negotiation of a single treaty, covering tariff, extra-territoriality, and inland water navigation, to replace the old Japanese Commercial Treaty. He subsequently gave up his insistence, however, and yielded to Mr. Shigemitsu's determination not to commit himself to more than one step at a time. Negotiations were accordingly begun for a substantive tariff treaty to supersede the provisional arrangement concluded in January 1929. The treaty, which was finally signed on the 6th May, while following in general the lines of the agreements made by the other Powers in 1928, represented a certain advance in that it introduced the principle of a conventional tariff. The Chinese Government undertook for a period of three years not to increase, or to increase only by $2\frac{1}{2}$ per cent., the duties on various articles in which Japan is specially interested, and received in return certain reciprocal tariff concessions.
- It will be remembered that the attempt of His Majesty's Government to secure a conventional tariff in 1928 had eventually to be abandoned and the new departure is therefore of interest. An exchange of notes attached to the treaty provided for the discontinuance after four months of the preferential rate of Chinese duty on goods imported or exported across the Korean land frontier. Other annexes contained an assurance with regard to the abolition of li-kin and a reference to Japanese unsecured debts. The latter one in which the Japanese have shown the strongest interest. The latter point is exchange of notes the Chinese Government referred to the setting aside of 5 million dollars annually for the consolidation of the unsecured debts (which the Japanese had secured in the course of their tariff negotiations the previous year—see China annual report for 1929), and stated their intention of calling a conference of credition on the 1st October. The insistence with which this assurance was followed up by the Japanese Government and the history of the Debt Conference which resulted are described in the financial chapter of the
- 206. A request for the rendition of the Japanese concession at Hankow was made to the Japanese Chargé d'Affaires in November, at the same time that a corresponding demand was addressed to the French Minister, but so far it has not been pressed.
- 207. In Manchuria equally the Japanese Government have avoided asserting themselves during the year. It is becoming increasingly hard to foresee the future of the Japanese Manchurian policy. Japan has openly maintained, as recently as at the Kyoto Conference of the Institute of Pacific Relations in 1929, that her special interest in Manchuria is based on essential considerations of national defence, as well as on economic grounds. But, if the present movement, which seems to be making for closer union between Manchuria and the rest of China, continues, it will be by no means easy for her to retain the strategic control which she built up upon the theory of Manchuria as an isolated area, for the security of which, in the event of Chinese civil war, Japan was responsible. For the present, she shows no intention of receding from her strongly entrenched position in the South Manchurian Railway area, and, indeed, one of the reasons which makes co-operation between her and the other Powers over the question of extra-territoriality difficulty, is her vital interest, of which she makes no secret, in securing reservations with regard to this area. She appears, however, to be intent for the moment on maintaining the status quo and avoiding the provocation of any controversy on the subject. Thus she refrains from any overt move towards extending her influence, whether political or economic. Her interests in railway development, and, in particular, in the Kirin-Kainei line, are not being pressed in any way, and she refrained rather unexpectedly from protesting against the contract signed in January with the Netherlands Harbour Company for the construction of a harbour at Hulutao, which was openly

designed to compete with Dairen. The only serious conflict between the Japanese and Chinese authorities in Manchuria occurred in the autumn in the Chientao area, near the Korean frontier, whence continued friction led to a clash in which two Japanese gendarmes were killed. The incident was settled by the payment of a small indemnity and the withdrawal of the reinforcements sent up by the Japanese, but the situation in the area contains the seeds of further trouble. The district is inhabited chiefly by Koreans, and the Japanese maintain not only four consulates but a number of police stations there, to which the Chinese naturally object, while the Japanese complain that the local authorities incite the Chinese to attack their Korean nationals and endeavour to foment Communist disturbances among them. As the Koreans continue to spread into Manchuria, carrying with them their Japanese extra-territorial rights, the whole question is a serious one, although the Japanese Government has now agreed that Koreans in China may divest themselves of their Japanese nationality, if they wish.

208. During the summer a Japanese Air Mission arrived in Mukden. Their contract was, however, only for six months, and their engagement does not seem to indicate anything more than the desire of Marshal Chang Hsueh-liang to obtain a certain amount of training for his air force on the cheapest terms available.

(5) Russia.

(a) Soviet Activities in China.

209. The year 1930 has again been almost devoid of any outstanding developments in Russian activity in China. In last year's report the opinion was expressed that, unless Soviet Russia once again found herself in a position to exercise direct control over the Chinese Communist party, further rot and disintegration would set in both in that party and its kindred Red organisations. Such has actually proved to be the case.

210. Conditions in the provinces south of the Yangtze are dealt with in another section of this report, and there is little doubt that in certain parts of Kiangsi, Hunan and Hupeh a definite Soviet régime has been actually established and Moscow's policy, in part at least, has been implemented. But it appears that Moscow is, in fact, far from satisfied with the situation which has developed throughout the year. Within the Chinese Communist party itself, there occurred a split of the first magnitude in June 1930, which has resulted in the formation of three different parties, each with its own policy. This split was the direct outcome of the differences in interpretation of the Third International's general policy of agrarian revolution in China generally and in the provinces south of the Yangtze in particular.

The Left Wing of the party, which is headed by Li Lieh-san, interpreted Moscow's instructions to mean revolution in its broadest senseinternational rather than national—accompanied by terrorism and industrial unrest, but unaccompanied by the consolidation of the power of the Chinese Soviet which was to be established as a result of this revolution. The Centre party, which is now most directly in touch with Moscow, interprets the latter's policy to mean national revolution before international revolution, and is strongly in favour of the policy of the consolidation of the power of the Chinese Soviet, as already established in certain provinces, before any steps are taken to give additional impetus to the revolutionary movement in this country. The Centre, it is true, supports the Red army and its activities, but attaches greater importance to the organisation and gradual bolshevisation of the masses than to winning either military victories or conquering further territory. It believes that the eventual Sovietisation of China depends upon the widespread dissemination of the principles of the Third International among the masses rather than upon instilling these principles into the narrower classes of labourers and peasants. Closely associated with the Centre in this doctrine are the Anti-Imperialist League, the various Oppressed Peoples' Associations and Youth Leagues, who guard against Government interference in their activities by professing nationalism as their creed. The Right party, headed by Chen Tu-hsiu, also believes in the theory of international revolution, as opposed to the immediate policy of Chinese agrarian revolution, but, at the same time, it is under no illusions as to the degree of success which is likely to attend its efforts in this direction at the present time.

- 212. It is extremely difficult to estimate the degree of direct support which Moscow gave to the Red armies during 1930. There seems to be no doubt, however, that during the early part of the year a considerable portion of the funds received by the Chinese Communist party from Moscow was, in point of fact, allocated to the use of the Red armies. This allocation is believed to have been discontinued after the middle of the year, and the Red armies in the field were left to fend for themselves and to supply the funds necessary for the conduct of their operations from the loot which they obtained from various cities and townships which they captured. It has been evident that at various times during the year the executive personnel of the Red armies was reinforced by the arrival from Russia of certain Chinese students who had completed their military training at the Sverdlov Academy in Moscow or at the Military Academy at Habarovsk.
- 213. With regard to the supply of arms to the Red armies, it is evident that the various nuclei around which these Red armies have grown were supplied in the first instance with arms received from Vladivostok and smuggled into the interior from the ports of Foochow, Amoy and Swatow. There are good grounds for believing that this traffic in arms, although still going on, has been reduced in volume, and the main source of supply of war material to the Red armies is now undoubtedly through direct capture in the field from the Nationalist forces opposing them or from deserters from those forces going over to the Red command.
- With regard to relations between Russia and Feng Yu-hsiang and Wang Ching-wei during 1930, there is little authentic information available. There is little doubt, however, that during the early stages of the Northern revolt Feng was definitely approached by emissaries of Moscow with the suggestion that he should give to this revolt a Red tinge in addition to its anti-Nationalist complexion, and it is known that there was constant and close liaison between the Comintern representatives in Tientsin and Feng's headquarters staff. But to all their entreaties Feng turned a deaf ear, largely because he undoubtedly did realise that his position as one of the dominant personalities in the Northern revolt was largely dependent upon the goodwill of Yen Hsi-shan, to whom he had to look for the supply of arms and munitions of war and to whom the Soviets were anathema. Similarly in the case of Wang Ching-wei. It is known that he was also approached by emissaries of Soviet Russia to give to the Reorganisation party movement, both before and after its identity with the Northern revolt, a definitely Leftist complexion. Wang Ching-wei refused to listen to any such suggestions, and was content to maintain, in company with the Northern rebels, the anti-Nationalist programme of his party. In the early part of the year information was obtained which showed that Soviet Russia was attempting to supply arms to Feng from Outer Mongolia, but it was never confirmed that these were supplied in sufficient quantities—if they were supplied at all—to make any material difference to the outcome of the struggle against the National forces.
- 215. It may not be out of place here to mention that during the year 1930 Soviet Russia was paying more attention to her colonial policy in the Far East than she was to her policy in China proper. There is little doubt that the Comintern was directly concerned with trouble in the Philippines in the middle of the year and with the trouble in French Indo-China which culminated in a series of armed outbreaks in September 1930. It is known that native agents working in her interests have been busy in Formosa, and definite information was obtained towards the end of the year that she was working out a programme aiming at closer liaison between the subversive elements in French Indo-China, Federated Malay States and the Dutch East Indies. Also there was definite evidence to show that the movement in French Indo-China was having considerable effect upon the internal situation in Yunnan, which assumed a definite Communist trend.
- 216. What the outcome of this colonial policy is likely to be remains yet to be seen, but it would appear that Russia has turned her attention now rather away from China proper and to the main land mass of South China comprising Yunnan, Kwangsi and Kwangtung and to the colonial possessions of the various foreign Powers in the South Seas. Whether or not she

will pursue her activities in this area and, with the growing strength of the National Government, leave China alone, depends very much upon whether the National Government is able to extract from her some binding promise with regard to the cessation of her Communist activities in this country at the Moscow Conference which is now being held.

(b) Chinese Eastern Railway.

- 217. With the signature of the Harbarovsk Protocol on the 22nd December, 1929, conditions on the Chinese Eastern Railway soon returned to normal. The Soviet employees who had been dismissed at the outbreak of the dispute were quickly reinstated, while the Sino-Russian board of directors, with a Russian manager in M. Rudyi, and a new Chinese president in Mo Teh-hui, resumed administration of the railway, in an atmosphere of harmony which, superficially at all events, continues to prevail. The damage done to the railway during the dispute was speedily repaired (Soviet troops in occupation of Manchuli are rumoured themselves to have participated in the repair work), and through traffic with Europe was opened on the 1st February. The marked restraint and civility with which the returning Soviet officials treated their lately vanquished foes undoubtedly contributed to the smoothness with which the line was again brought into operation; while it at the same time appears to have heightened in Chinese eyes the considerable prestige which the Union of Soviet Socialist Republics had lately won by the display of armed force.
- 218. It will be remembered that the terms of the Harbarovsk Protocol envisaged the calling of a conference at Moscow on the 25th January, 1930, which was to deal with all Chinese Eastern Railway issues still outstanding, together with the general question of the resumption of diplomatic and commercial relations between the Union of Soviet Socialist Republics and China. The holding of the conference was, however, delayed by the Nanking Government's refusal to ratify the protocol, on the grounds that the Chinese delegate at Harbarovsk had exceeded his instructions in allowing any reference to be made in the protocol to issues other than those immediately concerning the railway. The Nanking Government for long continued to maintain this attitude, and even when the Chinese delegation to the projected conference, headed by Mo Teh-hui, did eventually arrive in Moscow on the 9th May, the protocol was still unratified and the actual scope of the impending Sino-Soviet conversations unknown.
- 219. The next few months were passed in long negotiations between Mo Teh-hui and M. Karakhan on matters of procedure to be settled before the conference could formally open. The Russians insisted that the Harbarovsk Protocol should form the basis of the deliberations, while the Chinese took up their stand on the Mukden Sino-Soviet Agreement of 1924, under the terms of which the railway had been operated until the time of the recent dispute. The Russians appear to have made little attempt to accelerate these negotiations, but to have adopted the attitude that the railway question being already settled to their satisfaction, they could afford to deal with the other major issues at their own convenience; while Mo, being uncertain in the political confusion then prevailing, whether he was representing China or merely the Mukden Government, was no less reluctant to take the initiative.
- 220. With the liquidation, nevertheless, of the Northern rebellion led by Yen Hsi-shan and Feng Yu-hsiang, the Chinese delegation made a genuine effort to resolve the *impasse*. M. Karakhan, however, is reported now to have insisted that, as a condition of opening the formal conference, the Harbarovsk Protocol should not only form the basis of negotiations, but should also be ratified by the Nanking Government. He subsequently appears, however, to have dropped this second condition, and the conference formally opened on the 11th October with the Harbarovsk Protocol tacitly accepted by the Chinese as the basis of deliberations.
- 221. But M. Karakhan, in his first speech at the conference table, again endeavoured to force the Chinese into a formal recognition of the protocol. The attempt failed, and the conference broke down almost before it had begun. Long and tedious wrangles between the two delegations then ensued, largely over the

vexed question of the institution of negotiations regarding Sino-Soviet diplomatic and commercial relations. At last the Chinese appear to have given in, and the conference resumed its deliberations on the 4th December, after a "face-saving" compromise had been reached, whereby it was agreed that the existing conference should deal only with Chinese Eastern Railway matters, while the diplomatic and commercial relations of the two countries should form the subject of entirely separate, but presumably simultaneous, deliberations. In view of the extended scope of the negotiations, Mo Teh-hui informed the Soviet Government that he would be compelled to return to China to seek fresh instructions from his Government. The various technical sub-committees of the conference could, however, continue their work in his absence. He accordingly left Moscow on the 21st December and arrived in Harbin on the 29th December. On his arrival in China he is reported to have said that the validity of the Harbarovsk Protocol was no longer a live issue.

222. He left Harbin for Moscow at the end of March 1931, and it was expected that the Sino-Soviet Conference would resume its deliberations early in April.

(c) White Guards.

- 223. Much has been heard during the past year of the activities of so-called "White Guards" in North Manchuria. Most of these "guards" are Russian refugee settlers in Manchuria (and being refugees from the Soviet régime are of the "White" or Royalist persuasion), who have given up unprofitable farming for banditry, enlisting under the command of various bandit leaders. During the Sino-Soviet hostilities of 1929, these bands on several occasions joined forces with their kinsman settlers in the Three River and other districts to resist, sometimes with success, roving detachments of Soviet and Mongol raiders.
- 224. In spite of being sometimes boastfully referred to by the White Russian press in China as white "partisans" ready to release Russia from Soviet domination, &c., it is extremely improbable that any of these bands of marauders, who during recent raids upon villages along the western line of the Chinese Eastern Railway pillaged "White" and "Red" Russians and Chinese without discrimination, have any definite anti-Soviet counter-revolutionary objective, and they are in any case too small in numbers to be in any way effective.
- 225. The Soviet Government, however, though doubtless fully cognisant of the above facts, have been making as much capital as possible out of the presence of these armed "White Guard" bands in Chinese territory, presumably in the hope that they might eventually succeed in forcing the Mukden Government to entrust the protection of the Chinese Eastern Railway to Soviet troops. At all events, the Soviet Government in October, just prior to the formal opening of the Sino-Soviet Conference, addressed through their consul-general in Mukden a strong note to Marshal Chang Hsueh-liang, calling upon him to implement his obligations under the Harbarovsk Protocol by dissolving the White Bands and deporting their members from Manchuria.
- 226. The Mukden Government protested that the situation was in hand and that the bands would be ruthlessly suppressed. Nevertheless, despite these assurances, the bands, during the last months of 1930, seem to have continued their nefarious activities unchecked, and the powerlessness of the Manchurian authorities in the matter became evident when at the end of December it was reported that Peshkoff, one of the principal "White Guard" leaders, was in Mukden negotiating with the Manchurian Government the "honourable" surrender of himself and his followers, in consideration of financial aid to enable them to settle elsewhere.
- 227. This called forth yet another protest from the Soviet Government alleging that the Mukden Government was infringing the terms of the Harbarovsk Protocol, and it is possible that the whole question may be revived again when the Sino-Soviet Conference resumes deliberations.

(6) United States of America.

228. The new United States Minister, Mr. Nelson Johnson, presented his credentials on the 1st February. Four months later it was announced in the cess that he had submitted to the State Department a recommendation for the transfer of the American Legation to Shanghai. In the event nothing came of this proposal, which appears to have been suggested largely by the somewhat embarrassing position occupied by the Legations at that time in the territory controlled by the Northern faction in the civil war. Mr. Johnson, however, who is a bachelor, has himself spent the greater part of his time in Shanghai and Nanking.

229. The part played by the United States in the extra-territoriality negotiations is fully described elsewhere. In general, the insistence of the State Department on conducting the negotiations in Washington, which appears to be due to the determination of Dr. Hornbeck, the head of the Far Eastern section, to retain personal control of them, has seriously complicated for His Majesty's Government the task of maintaining a united front with America in this matter. The United States Legation have, however, co-operated with His Majesty's Legation to the best of their ability through full and frank exchange of all information available to them.

230. A treaty of arbitration between the United States and China was concluded at Washington on the 27th June. The treaty conforms to the standard model adopted by the United States and contains the usual reservation of matters within the domestic jurisdiction of the parties, or involving third parties, the Monroe doctrine, or China's obligations under the Covenant of the League of Nations.

231. There have been no other important developments in the policy of the United States in China, either financial or otherwise, during the year. America's wider knowledge of China, due to her growing commercial stake in the country and a corresponding increased interest in Chinese affairs, appears to have convinced both the public and the Government at home of the wisdom of going slow during the present period of political instability as regards both treaty revision and schemes of financial assistance. With respect to the latter, too much importance can hardly be attached to the salutary pronouncement made by Mr. Lamont at the Amsterdam Congress of the International Chamber of Commerce in July 1929, in which, in reply to somewhat uncalled-for protestations by the Chinese delegates that China would only accept foreign assistance in the economic reconstruction of the country on terms agreeable to herself, he stated bluntly that China's credit was at a low ebb owing to the disregard of her international obligations, and that, "until careful measures for its re-establishment have been taken by the Chinese Government, no loans on any scale calculated to be helpful could be made in the markets of New York."

(7) France.

232. A convention governing relations between China and French Indo-China, the discussion of which had begun in January 1929, was finally concluded after long and difficult negotiations on the 16th May. It gives the Chinese Government the right, which they have long sought, to appoint consuls at Hanoi or Haiphong and Saigon. Chinese citizens in Indo-China and French citizens in the three provinces of Yunnan, Kwangsi and Kwantung are, in general, accorded most-favoured-nation treatment in matters of trade, residence and travel, but the French authorities reserve in an annex the right to impose special taxes on Chinese in so far as they enjoy a traditionally privileged position in the country. In return, the French obtain certain rights to trade, reside and own property at places in the three limitrophe provinces. Ratification of the treaty has been held up pending the settlement of various outstanding questions.

233. Following the conclusion of the Agreement for the Revision of the Shanghai Provisional Court, the French authorities introduced on the 27th February certain modifications in the organisation of the Mixed Court in

the French concession. The only material change involved is that criminal cases in which there is no French interest are allowed to be tried by the Chinese magistrate without the participation of a French assessor (the assessor in purely Chinese civil cases had been withdrawn in 1926). This reform did not satisfy the Chinese, and in November the Minister for Foreign Affairs presented to the French Minister a draft agreement for the establishment of a Chinese court in the French concession on the lines of the Shanghai Court Agreement, but without a number of the safeguards contained in that instrument.

- 234. A strike of the utility companies in the concession, which broke out in June and disrupted communications for nearly three months, caused some anxiety to the French authorities in Shanghai, but was finally settled in August through the intervention of the French consul.
- 235. The French Government held aloof for the greater part of the year from the discussions on extra-territoriality, preferring to await the results of the British and American negotiations. They confined themselves to expressing readiness to consider concrete proposals from the Chinese. In November the Minister for Foreign Affairs handed to the French Minister a memorandum containing the outline of a proposed agreement which was the same at that presented to His Majesty's Government in the previous January. This was followed by the Chinese communication of the 17th December, complaining of the delay in the settlement of the question, and enclosing a formal draft on the lines of their November counter-draft to His Majesty's Government, to which the French Legation replied in the same sense as the rest of the Powers (see the section on Extra-territoriality).
- 236. In November Dr. Wang also approached M. Wilden with a request for the rendition of the French concessions and the territory Kwangchowwan. He referred in particular to Shameen and Hankow, and with regard to the latter produced a memorandum outlining conditions for the return of the concession modelled on the Chen-O'Malley Agreement of 1927. The nature of the French Government's reply is not yet known, but they do not anticipate any immediate pressure of this issue. No written communication passed on the subject of Kwangchowwan, but the French Government have informed His Majesty's Government that their attitude remains as defined in their declarations made in 1922, in which they expressed their willingness to rendite the Chinese territory under their control when other Powers should be prepared to do the like (citing in particular Kowloon and the Kwantung Territory).

(8) Germany.

- 237. As during the previous year, German influence in China has made itself felt chiefly through Chiang Kai-shek's German military advisers. At the beginning of May 1930 the strength of the Military Mission at Nanking under Lieutenant-Colonel von Kriebel was estimated at twenty-six officers, exclusive of civilian technical experts and police advisers; in addition, five German officers were employed in the Staff College at Peking. Further advisers continued to arrive from Germany from time to time. In June, von Kriebel, who was not popular with his colleagues, was succeeded by a General Wetzell as head of the mission.
- 238. As stated in the annual report for 1929, activities of the mission became increasingly embarrassing to the German authorities with the outbreak of hostilities between the North and South, especially as a number of the officers were actually employed at the front with the Nanking forces. Early in the year the German Minister, on the instructions of his Government, who foresaw the inevitable complications, addressed a formal protest to the Nanking Government against their employment of German nationals in this capacity. His representations were, however, rebuffed. On the other side, representatives of Marshal Yen Hsi-shan called upon Dr. von Borch in March to protest to him against the participation of his nationals on the side of Nanking, and later the Northern faction publicly announced that any German caught actively assisting the South in the civil war would be shot. Fortunately they were given no occasion for displaying the sincerity of this intention, against which the German Minister

naturally recorded a strong protest. It was probably intended mainly to discourage the participation in the actual hostilities of German aviators, which, to judge from the experience of the Sino-Russian campaign of 1929, might have been expected to have a serious effect on the fortunes of the war. In June the Northern Department for Foreign Affairs addressed a communication to His Majesty's Legation and the representatives of other signatories of the Treaty of Versailles protesting against the presence of the mission, as well as the supply to Nanking by Germany of arms and munitions, including poison gas, all of which were alleged to be contrary to the provisions of the treaty. No reply was sent by the Legations, and the German Minister, while rebutting the charges brought against his Government, pointed out to the Waichiaopu the solecism of appealing to a treaty which China had not signed. The German Government continued to disclaim the Military Mission and to deny the export of war material, and particularly gas, to China. As to the latter, it was, as usual, impossible to obtain conclusive evidence; and while it was reliably reported that extensive preparations had been made by the German experts at Nanking for the manufacture of poison gas with chemicals supplied from Germany, no reports were received of the actual use of gas by the Nanking armies.

The activities of the mission have an economic as well as a military They are believed with good reason to have the backing of the side Reichsverband der Deutschen Industrie; and as their technical assistance covers the erection of factories for war material, and according to the available information the scope of their advice embraces with German thoroughness questions such as the utilisation of civilian industries in war time, they have doubtless in the normal course of their duties been instrumental in securing a good deal of business for the German manufacturers. For instance, it was alleged by the Marconi Company and the Radio Corporation of America to be due to the influence of the Military Mission that the contract for a 50-kilowatt broadcasting station at Nanking was given to the German Telefunken Company, in spite of lower tenders submitted by their British and American competitors. The despatch of a German Economic Mission to China in the spring was also said to have been instigated by the military advisers at Nanking. This was, as far as the German Government was concerned, an unofficial mission composed of members of the above-mentioned industrial associations. It received, however, the full countenance and support of the German authorities. The commission arrived in Shanghai in April, and visited Nanking, Hankow and Canton, where they conducted a searching examination of the local industries. The civil war having then broken out, the scope of their official investigations was limited to the territory controlled by the Nanking Government, at whose invitation they had come, but unofficial visits were paid to Peking and Tientsin, and some days were spent in Mukden and Harbin before they returned home through Siberia. The main idea underlying their mission had without doubt been to examine the possibility of a large-scale development of Chinese industry with German co-operation. In this respect their visit came at an unfortunate moment (at least for the Chinese Government); since the political conditions at the time emphasised the unsoundness of any such scheme, even if Germany had been in a position to provide the capital without which it would not have been practicable. The chairman of the commission referred, indeed, to the financial stringency in Germany and to the withdrawal of American credits in a way which suggested that the possibility of drawing indirectly on the American market to finance their enterprise in China had not been far from the minds of the German industrialists. This idea does not seem to have been altogether abandoned, and one of the financial members of the commission travelled home through the United States with the object, it was said, of exploring the possibilities of obtaining American assistance; but in the disturbed state of affairs in China it is not surprising that nothing more was heard of this. Although there is as yet no sign that the mission has produced definite results of any importance, it has probably not been unfruitful in minor ways. The opportunity of a full first-hand investigation of conditions in China must have been of considerable value to the German interests concerned; valuable contacts must also have been established with those who control China's industrial development, who on their side can hardly fail to have been impressed by those contacts with a fuller idea of Germany' economic and industrial importance.

- 240. The negotiations entered into by the "Lufthansa" for the formation of a Sino-German company to operate an air mail service between Nanking and Berlin is dealt with in the chapter of the report concerning aviation.
- 241. Apart from their military and economic side, Germany's relations with China follow an unobtrusive course. Since the loss of her extra-territorial rights Germany has no outstanding political interests in this country. A certain amount of friction recurs from time to time over the treatment of her nationals. A particular case which attracted a considerable amount of attention during the year was that of Dr. Brietlander, a German doctor in Canton, who was sentenced to a year's imprisonment by the Chinese court for carrying out an autopsy on a Chinese hospital patient without the consent of the relatives. As, however, by the kind of compromise common in China, the sentence was not executed, the case had no serious consequences.

(9) Belgium.

- 242. The agreement signed in 1929 for the rendition of the Belgian concession at Tientsin was duly ratified by the Belgian Parliament in the summer of 1930. Exchange of ratifications and the formal rendition of the concession to China were, however, delayed by the failure of the National Government to implement their promise (made at the time of signing the agreement) to reimburse to the Belgian Government some 93,000 Tientsin taels in respect of outstanding debts incurred by the municipality of the concession.
- 243. Moved apparently, however, by a desire to secure the concession without further delay, the National Government early in 1931 finally agreed to pay up, and the formal ceremony of rendition took place at Tientsin on the 15th January.
- 244. The event, which was marred by the sudden illness of the Belgian Minister, was chiefly remarkable for the speeches of the Minister for Foreign Affairs and other Chinese officials, warmly praising the generosity of the Belgian Government in returning the concession to China; as a matter of fact, it had from the first been a liability, of which the Belgian Government were only too glad to rid themselves.
- 245. The only other event of importance in Sino-Belgian relations was the visit of M. Emile Vandervelde, president of the Second International, leader of the Belgian Socialist party and former Belgian Minister for Foreign Affairs, who arrived in Peking from Europe on the 3rd September on a lecture tour. In view of the civil war then in progress, the fact that M. Vandervelde's first official call after arriving in China was made upon General Yen Hsi-shan, occasioned some unfavourable comment.
- 246. After delivering several lectures before various Peking educational bodies M. Vandervelde left for Japan on the 14th September. He later visited and lectured at Shanghai and Nanking.

(10) Siam.

247. His Royal Highness Prince Purachatra, brother of the King of Siam, and Minister of Commerce and Communications in the Siamese Government, paid an unofficial visit to China in the autumn. His Royal Highness, accompanied by the Siamese Minister to Japan, arrived in Shanghai on the 9th October, and during his stay was entertained by the Chinese municipal authorities and by prominent Chinese residents. He afterwards visited Peking and Mukden, where he and his suite were the guests of Marshal Chiang Hsueh-liang.

(11) Denmark.

248. His Royal Highness the Crown Prince Frederick of Denmark, accompanied by his brother, Prince Knud, and Prince and Princess Axel of Denmark, visited Shanghai from the 9th to the 11th March, travelling on board

the motor vessel "Fionia," which had been placed at their disposal by the East Asiatic Company, of which Prince Axel is a director. The visit was an informal one, and their Royal Highnesses were only entertained by the Danish community. They sailed up to Nanking on the 13th March, where they were entertained by the President and the Minister for Foreign Affairs, and then left for a tour of Japan.

249. On their return from Japan the Crown Prince and Prince Knud, on board the "Fionia," paid a visit incognito to Weihaiwei, while Prince and Princess Axel spent two days in Peking. The fact that the Crown Prince did not accompany them was ascribed to the state of revolt of North China against the National Government, during which a visit by His Royal Highness might have been thought incorrect. The party sailed from Tsingtao for Singapore on the 2nd April.

250. The Great Northern Telegraph Company's agreements relative to the working of their cables in China were alleged by the Chinese Government to expire on the 31st December along with those of the associated British undertaking, the Eastern Extension Telegraph Company. Neither the Danish nor the British Legation intervened in the negotiations entered into by the companies for the conclusion of new agreements, which were not completed by the end of the year. Preliminary agreements were, however, signed on the 31st December which enabled the main cables at Shanghai and Tientsin to continue working.

(12) Treaties with Secondary Powers.

251. The Sino-Polish treaty concluded in September 1928 was not ratified by the Polish Government. They appear to have been dissatisfied with certain of its provisions, and the Polish delegate, M. de Weydenthal, was charged with the negotiation of amendments. These were embodied in an additional protocol (with exchange of notes) dated the 1st July, 1931. It is not apparent from the various points dealt with in the protocol what precisely were the objections of the Polish Government to the original treaty. The protocol lays down that either party may control immigration by non-discriminatory legislation. And it secures to Polish nationals the right, which in any case would hardly have come in question, to be tried by the so-called modern Chinese courts. Its main effect is, however, to emphasise the fact that Polish nationals in China are unreservedly subject to Chinese law.

252. A Sino-Czechoslovak Treaty of Amity and Commerce was signed at Nanking on the 12th February by the Minister for Foreign Affairs and the Czechoslovak delegate, M. Hnizdo. It follows fairly closely the lines of the draft commercial treaty handed to His Majesty's Minister in 1929, on which the Polish treaty was also based, in other words, the stock model which China has adopted as the type of an "equal" treaty.

253. A provisional commercial arrangement on the basis of reciprocal most-favoured-nation treatment was concluded with Egypt on the 23rd April through the Chinese and Egyptian representatives in London.

254. There was talk besides, during the year, of the negotiation of treaties with Finland, Turkey, Persia and Cuba. As the discussions in all these cases were carried on outside China, information was not available as to the progress of the negotiations.

255. None of these countries have interests of any importance in China, but their diplomats seem to share the eagerness of the Chinese to establish their position in the world by the negotiation of a treaty upon equal terms with anybody.

(13) The International Settlement at Shanghai.

(a) General.

256. A certain relaxation in the tension of the Shanghai atmosphere has been noticeable during the last year. This is probably a natural consequence of the time that has elapsed since the alarms of 1927, which led to the despatch of the Shanghai Defence Force. It reflects, however, to some degree the improvement in Sino-British relations, and, on the part of the Shanghai

community, possibly a slight increase of confidence in the policy of the British The Defence Force remains with a strength of two battalions, as Government. standing evidence of the concern of His Majesty's Government in the United Kingdom for the extensive interests at stake in the settlement, while the more responsible elements of the community are gradually coming to realise the inevitability of a policy of adaptation. In the course of his trips south in connexion with the extra-territoriality negotiations, His Majesty's Minister made a practice of visiting Shanghai and explaining the position to the Joint Committee of the China Association and the British Chamber of Commerce, and discussing with them, as representatives of the British residents, this and other questions affecting Shanghai; in these discussions little criticism was put forward of the Government's policy, which, whether they like it or not, the principal British interests in China now recognise as fixed. This change of mood was typified in the invitation extended to Judge Feetham at the end of 1929 to study and report upon the Shanghai problem. Judge Feetham arrived in Shanghai in January, and was given carte blanche for his investigation by the municipal council. This report, which it was expected would be published within a few months, was not completed at the end of the year, but he allows it to be understood that he has found the task of recommending a definite solution for the problem beyond him; and it is probable that, when the report appears, it will be useful mainly in ventilating the question by an exhaustive and impartial discussion of the facts. At any rate, Judge Feetham's investigation has possibly helped to keep the Shanghai question quiet during the year.

257. The municipal council gave a further indication of an altered spirit in their attitude towards Chinese representation. On the 1st January it was decided by the non-Chinese members of the council to propose, at the annual ratepayers' meeting, that the number of Chinese councillors should be increased from three to five, an increase which had been requested by the Chinese but refused the previous year. Unfortunately, the general meeting on the 16th April, which was poorly attended, rejected the proposal under the influence of an unexpectedly eloquent attack by a die-hard British lawyer. The Chinese had been led to regard the matter as settled (the Chinese Ratepayers' Association had actually chosen their five councillors), and it was generally feared that the rebuff must lead to a serious agitation; so much so that His Majesty's consul-general proposed, with the concurrence of the council, that the consular and diplomatic bodies should override the ratepayers' resolution and increase the Chinese representation under article 28 of the Land Regulations. It was decided. however, in the first instance, to call a special meeting of the ratepayers and endeavour to secure a reversal of the resolution, which the council considered was not representative of the real feeling of the community. This was successfully done at a meeting on the 2nd May, and a potential cause of serious trouble at Shanghai was thus avoided, the Chinese having in the meantime taken the matter very calmly in view of the measures which were known to be on foot to retrieve the ratepayers' initial blunder. The Chinese claim to further representation in proportion to the taxes paid by them in the settlement has not been pressed during the year.

258. The successful conclusion of the Shanghai Court Agreement (see below) helped considerably to clear the air of the settlement. The agreement was, indeed, adversely criticised at first in the foreign press, which expressed exaggerated fears as to the working of the new courts. The editor of the "North China Daily News," having first attacked the foreign Legations for concluding the agreement without consulting the council, was forced to change his ground, on the chairman, Mr. Arnold, refuting his statement, and transferred his campaign against Messrs. Arnold and Fessenden, the director-general (with whom various points had actually been discussed during the negotiations), with the result that the former failed to secure re-election to the council in March, his previous valuable services to the community apparently forgotten. Foreign misgivings proved, however, unjustified, and the new courts have, up till now, engendered less Sino-foreign friction in their working than the old.

259. A long-standing source of bitterness was happily removed by an arrangement reached in February for assuaging the memory of the 30th May incident of 1925. After long negotiations, through the Chinese members of the

council, with the association representing the relatives of the victims, the municipal council eventually paid over 150,000 dollars as a compassionate grant (as against the 75,000 dollars which had been offered in 1925), and a receipt was obtained accepting this in full satisfaction of all claims. (This did not prevent an attempt to stage a demonstration on the 30th May, which was, however, pusuccessful.)

- 260. The Chinese, on their side, have refrained from any serious agitation against the foreign control of the settlement itself. The question of the municipal council's outside roads continues, however, to be disputed. Contrary to the undertaking reached in 1926 for the maintenance of the status quo, the Chinese police, making use of their undisputed right to control the areas lying between the extra-settlement roads, continue to encroach on to these roads themselves, and a number of minor incidents have arisen in connexion with the patrolling and repair of the roads and the supply of light and water to adjacent premises. In December some alarm was caused by the stopping of foreign cars outside the settlement at the point of the revolver, though this was afterwards explained by the Chinese police to be part of a campaign against kidnapping. Neither the Chinese authorities nor the municipal council made any move to reach a settlement of the question of control, until the matter was taken up by His Majesty's consul-general, who eventually succeeded in impressing the council with the urgency of the matter. After some delay a suggestion was drawn up for the surrender by the council of the roads west of the loop-line railway, in return for control of the area up to the railway on the west, and some other agreed boundary on the north. The council were prepared to add certain financial inducements and to employ a Chinese police commissioner. These proposals, in short a measure of settlement extension, were communicated informally to the Mayor of Greater Shanghai by the Chinese councillors, but, before a discussion of them could be started, the latter met His Majesty's consul-general and informed him that they were inacceptable, and that, in any case, he had no power to possible a settlement of the question, which involved national issues. There to negotiate a settlement of the question, which involved national issues. the matter rested at the end of the year, though His Majesty's Minister continued to urge the necessity of seeking a solution locally.
- 261. It was decided, in the course of the negotiations for the modification of extra-territoriality, that it was essential to insert in the British proposals a clause providing for the exclusion of Shanghai from the operation of the new system, in order to secure the headquarters of foreign trade in China and to safeguard the vast interests centred there. This was done in the British draft of the 11th September, and the article reserving Shanghai and certain other areas is at present one of the main points under discussion with the Chinese Government.
- 262. It is, nevertheless, coming to be realised that the future of Shanghai lies in the gradual transfer of the settlement to Chinese control. A minor, but significant, development is a certain gradual and unobtrusive penetration of the settlement by means of the executive regulations of the Chinese Government. For instance, Chinese public health bureaux have recently been established by legislation with which chemists are bound to register. No attempt has been made to establish a bureau in the settlement, but it is understood that most of the Chinese druggists there have been induced to register with the Greater Shanghai bureau. This suggests the ease with which the foreign control of the settlement might eventually be undermined by entirely peaceful means.
- 263. On the top of the increase in Chinese representation on the council, the latter have decided to increase the Chinese element in their staff. They have also established a fund which is designed to compensate their foreign employees in the event of their at any time losing their posts under a Chinese-controlled administration.
- 264. The sale of the Electricity Department in 1929 has been followed by the disposal to another American group of the telephone system. This had been previously operated by a British Hong Kong company, who sold out in August to the International Telephone and Telegraph Corporation. As in the previous case, an outcry against the sale was raised in the Chinese press, and protests were even made by the Waichiaopu to the senior consul and to His Majesty's Legation

on the ground that the Shanghai Municipal Council had no right to grant, as they had done, to the purchasers a franchise extending for forty years. These objections were duly replied to, and nothing more has come of the agitation.

The question of commercialised gambling in the settlement was brought to the fore again by an application to the council for permission to introduce the Basque game of Hai Alai (pelota). The municipal police are the opinion that the existence of gambling places has contributed largely to the recent serious spread of crime at Shanghai, and a number of gaming houses have lately been closed by executive action on the part of the council. The application was therefore refused, but it was realised that the council was in a weak position for preventing the establishment of an enterprise of this kind without permission, as long as the (unlicensed) greyhound-racing clubs at Luna Park and the Stadium continued to operate. At the end of the year, therefore, the council, having been assured of the support of His Majesty's consul-general, were considering taking steps to close these British-owned dog-racing tracks. The companies owning them had been registered in 1927 by His Majesty's consul-general, and although repeated protests had been received from Chinese quarters against the encouragement of gambling at the dog races, the British authorities had hitherto taken the line that the legal difficulties in the way of suppressing them were insuperable. Mr. Brenan, however, now expressed the view, which was fully concurred in by His Majesty's Minister, that the activities of the companies were a discredit to us and the settlement, and that if the council were to take action against them they should have the fullest support which it was possible to give.

(b) Chinese Courts in the Settlement.

The negotiations for the revision of the Provisional Court Agreement of 1926, which had been begun in December 1929, lasted well into the year 1930 before a satisfactory conclusion was reached. They were conducted by a Chinese delegation led by Mr. Hsu Mo of the Waichiaopu, and on behalf of the foreign Powers by delegates appointed by the British, United States, French, Dutch, Norwegian and Brazilian Legations. On the foreign side the brunt of the negotiations was borne by the British delegation, consisting of Mr. Garstin, acting consul-general at Shanghai, Mr. Aveling, secretary of His Majesty's Legation, and Mr. Hewlett, consul-general at Nanking, with able assistance from the American delegates. The French held more or less a watching brief in the interests of their concession. The Japanese were not represented in the negotiations, as they were not among the Powers invited by the Chinese Government in their note of the 8th May, 1929. An attempt was made to get them included, and it was pointed out that owing to their participation in the control of the settlement, no agreement reached could be effective without their consent. The Chinese were, however, obdurate in refusing to admit them, on the ground that their jurisdictional treaty rights had expired, and the Japanese Government, who had shared fully in the preparatory discussions among the interested Powers, preferred not to delay the negotiations by pressing the matter.

Before the negotiations two draft plans had been drawn up by His Majesty's Legation and tentatively accepted by the heads of missions concerned, which were communicated to the foreign delegates for their information and guidance. The first provided for the replacement of the provisional court by a new special court with foreign co-judges on the bench, which it was hoped would, if the Chinese would agree to it, provide a really satisfactory judicial organ for the settlement; the second, which was included as a second string at the insistence of His Majesty's Minister, outlined a revision of the existing court in such a way as to meet the Chinese objections to the old system as far as possible without impairing the authority of the municipal council and its officers. Neither of these plans was actually presented to the Chinese, but the negotiations followed rather the lines contemplated in plan B, the course pursued by the foreign delegates being to attempt to graft the safeguards contained in this plan on to the proposals put forward by the Chinese, which aimed at the establishment of a purely Chinese court free from foreign interference. The chief of these safeguards were the application by the court of the Land Regulations and Bye-laws of the International Settlement, the participation of consular observers (which it was, however, agreed might be confined to cases affecting law and order and the

interests of the municipal council), a degree of foreign control of the judicial police, prisons and the officers of the court, the right of foreign lawyers to be heard, security against the abuse of Chinese procuratorial system, and the inclusion of some machinery for bridging over disputes between the court and the foreign executive authorities of the settlement. Most of these points were more or less hotly contested by the Chinese, and the negotiations had almost reached a standstill, when His Majesty's Minister arrived in Nanking in January and was able to get them under weigh again by personal discussions with the Minister for Foreign Affairs and the head of the Judicial Yuan on the chief outstanding points. It was eventually decided, after consultation with representatives of the Shanghai Municipal Council, to drop the system of consular representation (which had caused a good deal of friction in the working of the old Provisional Court) subject to the right of the council to be legally represented in all cases in which they claimed an interest. Insistence on a foreign clerk of the court was also abandoned, on condition that the processes of the court should pass through the hands of an officer of the judicial police nominated by the council. Satisfactory arrangements were reached with the Chinese on all the other points, and an agreement providing for the establishment in the settlement of a Chinese Special District Court and Branch High Court was finally signed on the 17th February.

268. The new courts came into being on the 1st April, and have functioned successfully during the rest of the year. The officers of the municipal council have experienced no difficulty in obtaining convictions in the majority of the cases prosecuted by them, and the special Sino-Foreign Committee set up under the agreement to smooth over difficulties arising between the court and the foreign executive has not been called upon to function. As regards civil cases, the record of the court is not so satisfactory, the chief subjects of complaint being the long delays of the law, the difficulty of obtaining execution of judgments, and some degree of corruption and racial bias.

III.—RAILWAYS.

Conditions on the Chinese railways at the close of the year presented an even blacker picture than they did twelve months earlier. The renewal of civil war on the grand scale in the summer of 1930 quickly put an end to the hopes that were entertained at the beginning of the year for the revival and rehabilitation of the railways in a new era of peace and prosperity. Once again, as these words are being written, the dawn of a new year gives promise of rehabilitation and reform, but the damage is now still more costly to repair, and money is even harder to find than it was a year ago. The prospect of funds being made available from the British indemnity settlement for the reparation of some of the old lines, as well as construction of new ones, is the one bright spot in the picture. In other respects, the outlook is one of unrelieved gloom, for not only has the recent civil war given a rapid impetus to the process of disintegration of several of the main railways, but the sensational fall in the value of silver has practically doubled their gold obligations and the cost of renewals of materials, and the prospect of placing the railways, many of which are bankrupt, on a sound financial footing is correspondingly remote. At a conference held early in 1931 the Minister of Railways is reported to have assessed the cost of rehabilitating the existing lines at no less than 1,000 million dollars (this high figure is presumably meant to include payment of the financial obligations of the railways). several of the main trunk railways have been operated in sections under the control of various leaders. Even at the close of the year, when peace had already been declared for several months, large quantities of rolling-stock were still in the hands of recalcitrant military leaders, some of whom were running independent services of their own on sections of the lines. The Ministry of Railways have estimated the losses to the railways in the recent civil war at 73 million dollars, and actual military requisition from the railways during the period at over 4 million dollars, probably a conservative figure and not inclusive of military fares and freight unpaid. Even if the Ministry of Railways should succeed in wresting the control of the lines from the various military commanders, which at present seems unlikely to happen for some time to come, the task of reform

Numerous abuses have thrived unchecked during the will be no simple one. frequent periods of civil war. Corruption is rampant in the various railway administrations, the heads of which are often under the influence of some military chieftain or other, and are liable to be constantly changed. In many cases, they are men who have had no previous experience of railway administration. Cars are frequently put up to auction by the militarists themselves, and the merchants requiring freight space for their cargoes are at all times at the mercy of the transportation companies, who have no regular tariffs but sell such space as they can command to the highest bidder. Until the Chinese Government railways are brought under the control of the Ministry of Railways, or whatever department of the Government is designed to administer them, and are operated by staffs owing allegiance to nobody but the Government itself, and having direct control over all the operations of the line entrusted to them, the evils of the present system, or lack of system, will continue to have a disastrous effect on the trade of the country. This is particularly true of the export trade. Chinese products have to face strong competition and constant price fluctuations in the markets of Europe and America. The present uncertainties of transport in this country, coupled with the numerous tax exactions still collected on the railways, frequently raise the price of Chinese commodities at the port of export higher than the price obtainable abroad, and exporters are constantly unwilling to assume any risks of financing cargo from the interior to the treaty ports.

- 270. Not the least of the difficulties with which the Chinese railways have had to contend during the past year is that of bandit "raids," which are, of course, an indirect result of civil war conditions. It is no exaggeration to say that no railway in China is safe from this scourge.
- 271. Statistics prepared by the Ministry of Railways in June 1930 give the total length of railways in operation in China (excluding the two remaining "concession" lines, the Chinese Eastern and the Yunnan Railways) as 12,335 kilom.
- The outstanding liabilities of the Chinese Government railways to British firms for materials supplied and not paid for are no nearer a settlement, in spite of strongly-worded representations and constant pressure on the National Government by this Legation, and the endeavours of the firms themselves through These debts now stand at a their own representatives, to obtain satisfaction. The case of Messrs. William Forbes silver figure of over 30 million dollars. and Co., of Tientsin, who are now in serious straits owing to the fact that they are owed over 3 million taels for the five Blue Trains supplied to the Tientsin-Pukow Railway as early as 1921, was taken up at Nanking by Sir Miles Lampson and Mr. Ingram with the Minister for Foreign Affairs and the Minister of Railways personally on numerous occasions during the year but without result. The attitude of the Government representatives was invariably that it is impossible to draw blood out of a stone. It appears improbable that it will be possible to obtain even a fractional payment on account of these large debts until the railways concerned have been set on their feet again during a prolonged period of peace, when the assurance given by the Chinese Government, which is appended to the British indemnity settlement, can be invoked, for what it may be worth, as a lever in renewed insistence on the liquidation of these debts. To all representations regarding the now extremely heavy defaults in respect of railway loans, the Ministry of Railways returns the unvarying reply that it is engaged in devising plans with a view to a general readjustment (see also clause 5 of the proposals put forward by the Chinese Government at the informal debt conference held at Nanking on the 15th November, 1930, in the section of this report dealing with "Finance.")
- 273. In regard to the loans and advances made to the Chinese Government, in which the British and Chinese Corporations (Limited) and Chinese Central Railways (Limited) are interested, the position as at the 31st December, 1930, showed that out of total loans and advances, amounting to £23,442,761, a sum of £17,818,796 was still outstanding. Of this, £4,129,680 represented payments of principal in default, and £3,258,894 payments of interest in default, making a total default of £7,388,574.

274. An outstanding example of the extremely nationalistic policy adopted by the present Government, is to be found in the discriminatory freight rates for the carriage of goods by the Chinese railways, according to whether the goods are native goods, or goods imported from abroad or manufactured in China, by firms operated by foreign capital and enterprise. These discriminatory rates were he outcome of the issue of a so-called "General Classification of Goods" issued by the Ministry of Railways in January 1930, and affected not only the actual freight rates but taxation collected locally on certain railways proportionate to the freight paid. A protest against this system was made by the Senior Minister acting on behalf of the foreign representatives to the Minister for Foreign Affairs in June 1930, in which it was pointed out that not only was the system totally opposed to international practice and international comity, but that it was a breach of article 5 of the Nine-Power Treaty signed at Washington in 1922, which stipulated non-discriminatory treatment on the Chinese railways. Chinese Government did not see fit to reply to these representations, and complaints of discriminatory treatment were still being received from foreign concerns at the end of the year. The Minister of Railways has, however, since declared that he does not approve of the system, and that it is the intention of the Government to abolish it.

275. Through the intermediary of Mr. J. W. Lockhart, a British subject who occupies the post of financial and statistical adviser to the Chinese Ministry of Railways, as well as that of chief accountant of the Shanghai–Nanking Railway, and who was on leave in England during the past year, liberal proposals were agreed upon with the management of the London, Midland and Scottish Railway for the practical training of railwaymen from the Chinese railways, not to exceed twenty in number at any one time. The British railway also agreed to second railway specialists for service on the Chinese lines for periods not exceeding two years. These proposals were put before the Ministry of Railways on Mr. Lockhart's return to China, and it remains to be seen whether anything will come of them. Their execution would serve as an admirable counterpoise to the existing preponderating American influence in Chinese railway affairs.

Peking-Mukden (Peiping-Liaoning) Railway.

276. The affairs of this railway have during the past year been under the directorship of General Kao Chih-yi, an adherent of Marshal Chang Hsueh-liang, and said to have considerable influence with the latter. He is a person of arrogant manners, who will stop at nothing to gain his own ends, and representatives of British interests bound up with the railway have found him exceedingly difficult to deal with. It is also noteworthy that all efforts to persuade the young marshal to bring pressure to bear on him have been unsuccessful. Removed from the immediate area of civil war, this line has had a more successful financial year than the majority of the Chinese railways. The Railway Administration has, however, shown no disposition to utilise its surplus earnings to wipe off its still considerable debts to British concerns, either for railway materials supplied or on account of defaulted loan obligations. A series of representations were made by this Legation in regard to a contract entered into by the Railway Administration in January 1930 with the Netherlands Harbour Construction Company of Amsterdam for the completion of the Hulutao port project (Hulutao is a harbour on the coast of the Gulf of Pechili to the north of Shanhaikuan, which is said to have great natural advantages, and which the Chinese have for years past aimed at making into a rival to Dairen). contract stipulated for payments to the Dutch concern of a sum of 6,400,000 gold dollars, at the rate of 95,000 gold dollars a month, for construction of the harbour, the work to be completed in five and a half years (by April 1935). A monthly contribution of 500,000 dollars was to be allotted for the purpose from the earnings of the railway. Protests from this Legation were based not only on the fact that the contract constituted a breach of article 5 of the Railway Loan Agreement of the 10th October, 1898, which stipulates that no further loan shall be charged on the revenues of the railway, except through the British and Chinese Corporation, until the main loan has been redeemed, but that various other obligations, additional to the original loan of 1898 and of the Double-Track Loan, advanced by the corporation in 1921, were in default. These obligations

are in respect of the Peking-Mukden Railway Loan (Fixed Deposit), the Shanghai-Fengching Railway Mortgage Redemption Loan Agreement of the 14th February, 1914 (arrears of principal and interest and Fixed Deposit—an obligation which the Peking-Mukden Railway Administration have since 1926 refused to recognise on the ground that repayment is the concern of the Shanghai-Hangchow-Ningpo Railway, which benefited by the loan), and the Shanghai Hangchow-Ningpo Railway Loan Agreement of the 9th March, 1908 (Fixed Deposit), while large sums are still owing to British creditors for rolling-stock. The total repayment of the loan for the double-tracking of the line from Tongshan to Shanhaikuan of 1921 should have been repaid, as to its sterling portion in May 1927, and as to its silver portion in July 1926. Arguments based on these defaults failed, however, to move the Railway Administration, which declared that the harbour contract was not a "loan" in the sense of the loan agreement of 1898, and that it was, in fact, merely an item of construction work, like any other, for the development of the line. Recent information indicates that, in spite of the usual setbacks and squabbles, the Hulutao scheme is being pushed on apace. When the present contract is completed, however, considerable construction of wharves, godowns and buildings will be necessary before the port is a going concern, and the prospect of its becoming a serious rival to Dairen is remote—a fact which has no doubt caused the Japanese to refrain from protesting against the scheme on political grounds. Further grievances of the British and Chinese Corporation against the railway arose from the allocation of an additional 100,000 dollars a month of the railway's earnings to the construction of the Tao-Shan Railway in Manchuria, while another 100,000 dollars a month was to be devoted to the southern (Kwangtung) section of the Canton-Hankow Railway, and from the now common practice of depositing the railway revenues in Chinese banks in Tientsin and Mukden instead of in the Hong Kong and Shanghai Bank, as called for by article 8 of the loan agreement of 1898. The root of all these difficulties in regard to the Peking-Mukden Railway is that it is not within the effective control of the Nanking Government, but of the Mukden authorities, though the Ministry of Railways at Nanking is nominally responsible for it. Both Mukden and Nanking can, therefore, disclaim responsibility for the Railway Administration's actions. This state of affairs is also largely to blame for the detention throughout the year of large quantities of rolling-stock belonging to other Chinese railways on the section of the line outside the Wall (in Manchuria). While the Railway Administration is at Tientsin, the directorgeneral himself is usually absent in Manchuria. The uncompromising attitude of the railway directorate towards its British employees has been shown in its refusal to grant any adequate compensation to these employees in respect of the heavy depreciation in silver (they are now paid at the rate of 12 dollars to the £1), which has caused the sterling value of their emoluments to shrink to little more than a half of what it was a year ago, and has consequently inflicted serious hardship, particularly on the men who have financial commitments (families, &c.) at home in England. Many of these men were originally engaged on a sterling basis, but their actual contracts have lapsed and not been renewed, thus weakening the legal basis of any claim they may have on this score. In their policy of gradual replacement of the foreign staff by Chinese, the railway directorate refuse to consider an increase in the silver salaries of their foreign and not those of their Chinese employees, though the effects of the fall in silver exchange is, of course, in no way comparable in the two cases. Constant representations by His Majesty's Minister, whether to the Nanking Government or to Marshal Chang Hsueh-liang, have failed to move them from this standpoint.

277. The railway has suffered seriously during the year from wash-outs caused by floods.

278. The silver portion of the Double-Track Loan of 1921 was extinguished in August 1930. Since that time the railway has continued the minimum monthly instalments of £10,000 stipulated in the agreement towards the repayments of the sterling portion, and has promised to continue payment of an additional sum of 50,000 dollars monthly (as prior to the extinction of the silver portion) commencing from September last; payment of this latter amount has since, however, constantly been delayed. The efforts of the British and Chinese Corporation, backed up Sir Miles Lampson's personal representations to the young marshal, to

get these instalments increased to £25,000 a month have been unsuccessful. At the present rate of payment, the loan will not be finally repaid till 1933, or six years after due date.

279. Mr. Farrant, the senior British district engineer on the railway, was elieved of his position in October 1930, the Railway Administration being dissatisfied with his conduct in connexion with the repair of wash-outs that had occurred on the line near Peitaiho in August. Mr. Farrant had spent twenty years in the service of the railway, and his appointment as deputy engineer-inchief was officially notified by the Ministry of Railways in December 1928, though never ratified by the director-general of the railway. The arbitrary manner of Mr. Farrant's dismissal was typical of the treatment recently accorded to the foreign employees of the Chinese railways.

Tientsin-Pukow Railway.

- 280. The accumulated defaults on the original loan of 1908 for the building of this railway (British portion) amounted at the end of the year to £754,600 11s. 1d., and on the Supplementary Loan of 1910 (British portion) to £578,643.
- 281. The vexed question of the substitution of the customs revenues for *li-kin*, on the abolition of the latter form of internal taxation, as security for the payment of these loans, in accordance with article 9 of the Supplementary Agreement of 1908, and article 9 of the Supplementary Agreement of 1910, was still unsettled at the end of the year, the Ministry of Finance having come to no decision in the matter. The position is the same in regard to the similar assurance given in article 9 of the Hukuang Railway Loan Agreement of 1911.
- 282. The British chief engineer, Mr. A. R. J. Hearne, the only remaining foreign engineer on the railway, retired at the end of the year after twenty-two years' service on the line. His wife had previously been the victim of a savage assault by a soldier in uniform at their railway residence at Puchen, near Pukow, the southern terminus of the line, on the 5th August. In view of the arduous and valuable nature of Mr. Hearne's services to the railway through successive periods of civil war, Sir Miles Lampson pressed his claim for adequate financial treatment on retirement very strongly with the National Government, and finally terms acceptable to Mr. Hearne were obtained.
- 283. Through traffic on the railway was suspended for the greater part of the year owing to the fact that it was the main line of communication for both the Northern and Southern armies throughout the period of civil war. It was only resumed early in November.

Canton-Hankow Railway.

- 284. The arrears on the Hukuang Railways Loan of 1911 amounted at the end of the year to £1,749,328 18s. 1d., exclusive of interest on bonds drawn for payment, but unredeemed at due date.
- In September the managing director of the railway issued an order dismissing Mr. F. W. W. Valpy, the British engineer-in-chief, and sole remaining British engineer, of the Hupeh-Hunan section of the line, on the ground that there was no longer any necessity to employ a foreign engineer-in-charge. Mr. Valpy was concurrently acting engineer-in-charge of the Chuchow-Pinghsiang Branch Railway, in accordance with the letter of agreement of the 31st March, 1914, between the Ministry of Communications and the British and This letter was supplementary to article 2 of the Chinese Corporation. Nanking-Hunan Railway Loan Agreement of the 31st March, 1914, providing for the incorporation of this branch line as an integral part of the railway to be constructed. Later (in 1928) the administration of this line was amalgamated by the Chinese with that of the Hupeh-Hunan section of the Canton-Hankow Railway. The Group Banks protested against the managing director's statement that there was no longer any necessity to employ a foreign engineer-in-chief, as being in contradiction to the express terms of article 17 of the Hukuang Railways Loan Agreement of the 20th May, 1911. The French and American Legations

joined this Legation in making representations to Nanking against this infringement of the loan agreement, and the Chinese Government were urged not to dispense with Mr. Valpy's services till they had fulfilled their financial obligations, which were heavily in arrears, towards him. The matter was finally settled by payment to Mr. Valpy of the arrears due to him, and the seconding of Mr. J. C. Steen, a British engineer on the Peking-Mukden (Peiping-Liaoning Railway to be acting engineer-in-charge of the Hupeh-Hunan and Chuchow-Pinghsiang lines. It is reported that the Railway Administration have endeavoured to persuade Mr. J. H. Williams, former British engineer-in-chief of the line, to return to the post, but that the salary offered did not satisfy him.

- 286. Considerable quantities of railway material for the southern (Canton-Shiuchow) section of the railway continue to be purchased out of remitted Belgian indemnity funds, and work on the section from Shiuchow to Lokehong is being pushed forward.
- 287. The construction of the loop-line connecting the Canton-Hankow and Canton-Kowloon railways has still not been begun.

Canton-Kowloon Railway.

- 288. After consultation between the departments concerned, it was decided that the claims of the British section of the railway against the Chinese Government for compensation in respect of suspension of traffic on the Chinese section during periods of civil disturbances, based on article 7 (f) of the Canton–Kowloon Railway Joint Working Agreement of the 8th September, 1911, were legally weak and the ultimate chances of recovery slender, and that it would be unwise to press them. These claims have been therefore tacitly dropped. The Hong Kong Government considered that it would be impolitic to suggest to the Chinese Government any revision of the working agreement so as to put the losses in respect of suspension of through traffic on a more definite footing, as the first thing the Chinese would demand in any such negotiations would be a revision of the ratio of 65:35 by which the takings of the through traffic are divided between the British and Chinese sections.
- The state of the track on the Chinese section of the line became so bad during the year that the journey between Canton and Hong Kong by train took five and a half hours, as against four hours, and was thus only a fraction quicker than the passage by steamer. The British engineer-in-chief at Canton, Mr. W. M. Stratton, had great difficulty in persuading the managing director to purchase the necessary new sleepers, failing which the speed of the through trains would have to be reduced from 30 to 20 miles an hour, and the new express locomotives, purchased under the agreement with the Hong Kong Government in 1929, would be useless. The necessary order for Australian sleepers was finally placed by the Purchasing Commission of the Ministry of Railways at Nanking for delivery between November 1930 and April 1931, though His Majesty's consul-general at Canton subsequently reported that owing to what appeared to be unwarranted delay on the part of the Purchasing Commission in agreeing to the terms of fulfilment of contract offered by the Australian suppliers, with whom the railway had transacted business satisfactorily for years past, the despatch of the sleepers had been indefinitely postponed. The matter was in the end taken out of the hands of the Purchasing Commission by the British chief accountant of the Shanghai-Nanking Railway Administration, by which the funds for the purchase of the sleepers were being advanced.
- 290. The defaults in respect of the Canton–Kowloon Railway Loan of the 7th March, 1907, amounted at the end of the year to £820,709 $2s.\ 8d.$

Shanghai-Nanking Railway.

291. A default occurred in payment of the second instalment of the redemption of the Shanghai–Nanking Railway Loan of 1903, which became due on the 18th May, 1930, for payment to the bondholders on the 1st June. The amount was £116,290. A temporary default also occurred in payment of the half-yearly interest on this loan, to the amount of £69,774, payable on the 17th November. This default was, however, quickly rectified by payment, to the British and Chinese

Corporation in London, through the agents of the National City Bank of New York, of £60,000 on the 16th December, while the balance of £9,774 was eventually remitted by the railway through the Hong Kong and Shanghai Bank in the usual manner. The representative of the corporation in China saw fit to protest to the Ministry of Railways, on the strength of article 15 of the Loan Agreement of 1903, against payment of the remittance of £60,000, otherwise than through the Hong Kong and Shanghai Bank in Shanghai.

- 292. The unsatisfactory financial position of the railway was partly brought about by the heavy depreciation of sterling exchange, and partly by the loss of through traffic from the Tientsin–Pukow Railway owing to the civil war, although the railway itself was fortunately removed from the actual scene of military operations. A considerable increase in working expenses and expenditure on new works has, however, borne witness to unsatisfactory conditions of operation and lack of foresight on the part of the administration. There has also been considerable military interference in the locomotive department in connexion with the construction of armoured trains, immobilising cars required for public traffic and preventing the execution of repairs. Wagons have been held up for long periods loaded with military stores, while no payment in cash for any military traffic or for the removal of rolling-stock for military purposes has been made.
- 293. A formal ceremony took place at Nanking on the 1st December to mark the beginning of work on the Pukow-Nanking Railway ferry, which will eventually link up the Tientsin-Pukow and Shanghai-Nanking lines. It is said that the ferry will be designed to carry complete trains of ten cars with a locomotive, and that the service will be inaugurated in about a year's time. The scheme, which is estimated to cost 4 million dollars, is to be financed by the Ministry of Railways itself. As far as is known, no contracts have as yet been awarded in connexion with the scheme.

Peking-Hankow and Lung-Hai Railways.

- 294. These lines have, like the Tientsin–Pukow Railway, been made to suffer the full force of civil war conditions throughout the year, and commercial traffic has been operated only in sections. Both lines are in a terrible state of disrepair, and will require a very large expenditure to restore them to anything like normal conditions. Through traffic between Peking and Hankow was resumed towards the end of the year, only to be quickly interrupted by bandit raids in Honan. The rolling-stock is of the poorest description. The head office of the railway has recently been removed from Peking to Hankow. The Lung-Hai line is said to be now running westwards as far as Lingpao on the Yellow River in Honan, and light rails have been pushed forward to T'ung-kuan on the Honan–Shensi border.
- 295. The Manchurian railways are dealt with in the section of this report under the heading "Manchuria."

IV.—FINANCE.

296. The financial barometer at the opening of the year showed a rising tendency, and prospects looked brighter than they had been for years past. The new tariff had produced a huge increase in the customs returns, and the revenue from the Salt Administration under the new machinery had exceeded all expectations. Moreover, a further expansion of the customs revenue was anticipated from the introduction of the new gold unit (referred to in last year's report) on the 1st February, 1930. The reports of the Kemmerer Commission were also being investigated by the Government and schemes of financial reform were in the air, while to all appearances there were no war clouds on the horizon. The atmosphere, however, was charged with electricity, and the storm broke in April, when the State Council promulgated a mandate ordering the arrest and dismissal of General Yen Hsi-shan. The ensuing civil war upset all hopes of financial rehabilitation, and the resources of the Government were taxed to the utmost to provide the sinews of war for their campaign against the North. Heavy

inroads had already been made upon the increased customs revenue, but under pressure of war further loans were squeezed from this source. The salt revenue, too, which in a recent statement was said to have amounted to 122 million dollars for 1930, must have been largely used to finance the campaign. Nanking's ultimate victory was therefore a costly business, and the Minister of Finance has publicly announced that the deficit for the fiscal year, which ended on the 30th June, 1930, amounted to approximately 100 million dollars, and that next year's deficit may be expected to be even larger.

Domestic Loans.

297. Domestic loans have been the lifebuoy of the Nanking Government since its inception, and they made good use of this method to keep themselves afloat during the year under review, as the following list of loans indicates:—

Date of Issue.	Amount.	Interest.	Name.	Security.
	Dollars.	Per cent.		ACTIONS INTO COMM
January 1, 1930	20,000,000	8	19th Year Customs Revenue Bonds	Customs.
March 1, 1930	24,000,000	9.6	19th Year Treasury Bonds	Rolled tobacco tax
September/October 1930	80,000,000	9.6	19th Year Short Term Treasury Notes	Customs.
October 31, 1930	50,000,000	9.6	19th Year Rehabilitation Loan	Customs.

This brings the total of domestic loans issued by the present Government from the 1st May, 1927, to the end of 1930 to 592 million dollars, all of which are being successfully administered under the punctilious care of the Ministry of Finance, and one cannot but feel that if the same standard of energy and ability in the faithful observance of contractual obligations were extended to the foreign loans, there would be a different tale to tell.

- 298. The four loans quoted above are those for which the Government have definitely accepted responsibility, but there are many others which have been submitted to or passed by or adopted in principle by the Government whose fate is unrecorded. Among these are the following:—
- 299. In January a scheme for a 50 million dollar loan was submitted to the Executive Yuan by the Ministry of Industry, Commerce and Labour, to be devoted primarily to the opening of cotton mills and salt and sugar refineries. The loan was to be secured on the increased customs revenue.
- 300. In March a proposal relating to the issue of a public loan of 30 million dollars, and an additional assessment of 20 million dollars, from the various provinces for the reconstruction of Nanking, was adopted in principle by the Central Executive Committee. This loan was to be a further charge on the increased customs revenue.
- 301. About the same time the regulations of a 10 million dollar Telegraph Administration Loan were published, the security for which was to be the entire revenue from all international messages despatched by the Ministry of Communications.
- 302. In April the National Famine Relief Committee submitted a petition to the State Council recommending the collection of a famine relief surtax of 10 per cent. on the customs duties and the issue of a domestic loan of 20 million dollars to be secured on the returned Boxer indemnities. Some doubts seem to have been entertained by the petitioners as to the reception which might be accorded to the proposed domestic loan, and it was therefore suggested that, in the event of it being impracticable, a foreign loan should be floated on similar lines. The Executive Yuan's response to this petition was to give instructions to the Ministry of Finance that steps should be immediately taken for the issue of a 10 million dollar loan for famine relief, secured on the levy of a customs surtax, but there is no record of the loan having been issued.

- 303. This was followed in May by a scheme for the building of twenty-four new vessels for the China Merchants Steam Navigation Company, which would necessitate the raising of a public loan of 20 million dollars, half of which was to go towards liquidating the outstanding debts of the company.
- 304. In June a Chekiang Provincial Loan of 1 million dollars was uthorised by the Legislative Yuan for famine relief purposes secured on the provincial revenue.
- 305. Towards the end of August regulations were issued for a Kiangsu Provincial Reconstruction Loan of 7 million dollars, secured on revenue derived from that province, and in December the Legislative Yuan published the terms of a 5 million dollar Locomotive Loan for the Peking–Mukden Railway, which was underwritten by a Chinese banking syndicate. It was stipulated that the funds required for the service of this loan were to be appropriated monthly by the Railway Administration out of the increased revenue resulting from the new fleet of locomotives, and any deficit was to be made good by the Administration.
- 306. It will be seen from the above list that there has been no lack of activity during the past year in the domestic loan market, and there are indications that the current year will be equally fertile in loans of this description.
- 307. The new year was, in fact, ushered in with a National Loan of 60 million dollars, secured on the tobacco tax, and called "20th Year Rolled Tobacco Treasury Notes," the rate of interest being 7 mille per month. i.e., 8.4 per cent. per annum.
- 308. The flotation of a 10 million dollar loan, for the development of coast and inland navigation and the rehabilitation of the China Merchants' Steam Navigation Company, has also been agreed to in principle by the Government, and the regulations are to be submitted to the Legislative Yuan for approval. This is presumably the offspring of the scheme proposed in May 1930 for the same purpose.
- 309. It would almost seem as if a policy of issuing loans for the development of domestic industry was about to be inaugurated, as a recent announcement states that the Ministries of Industry and Finance are co-operating in the issue of a 15 million dollar loan for the organisation of five Government factories, namely, a textile factory, a woollen mill, a salt and sugar refinery, and a chemical works. This proposed loan also seems to have something akin to that of the 50 million dollar scheme already referred to, which was submitted to the Executive Yuan in January 1930.
- 310. Provincial loans seem to be growing in favour, and in February of the current year the Legislative Yuan passed regulations for the issue of the 20th Year Hupeh Provincial Rehabilitation Loan of 3 million dollars, secured on revenue from the province, and bearing interest at 8 per cent. per annum.
- 311. All these loans, however, were put in the shade by the announcement of another National Loan of no less than 80 million dollars, for the security of which the customs revenue is once more called into requisition. The loan is to be known as the "20th Year Customs (Duty) Short-Term Treasury Notes," and it is said that the proceeds will be used to make up the deficit of the Government for the current year. Interest is at the rate of 8 mille per mensem (9.6 per cent. per annum), and redemption is to be completed in 100 monthly instalments, terminating at the end of July 1939. Article 6 of the regulations lays special stress on the funds required for the service of this loan being "definitely earmarked by the Minister of Finance from the increased customs revenue," and the Inspector-General is to be "specially instructed to remit and deposit monthly with the Central Bank the requisite amount."

Foreign Loans.

312. As might have been expected from the large increase in the customs revenue, no difficulty was experienced in meeting the so-called "Customs Loans," but, owing to the heavy slump in silver, some misgivings arose towards the end of the year as to the future of the gold obligations. These apprehensions were accentuated when early in February of the current year, Mr. Hussey-Freke, the

Associate Chief Inspector of the Salt Gabelle, was superseded by Dr. Frederick A. Cleveland, an American, who was publicly reported to have suggested that the Government should declare a moratorium on Chinese Gold Loans. There is reason to believe that this report was not unfounded, but, observing the effect that it had on Chinese bonds on the London Stock Exchange, Mr. T. V. Soong was astute enough to announce that the "circulation of this rumour" was unwarranted, and the bonds gradually recovered their equilibrium.

- 313. The salt loans were less successfully maintained, but due credit must be given to Mr. Soong for regaining a hold on the salt revenue and taking practical measures to remedy the defaults on the loans secured thereon. At the close of 1930 only one instalment, amounting to £250,000, of the Anglo-French Loan was in arrears, and the Crisp Loan, though still somewhat in default as regards redemption payments, was brought up to date in the payment of its interest coupons. The June coupon of the Hukuang Loan was also paid, the sum required exceeding the amount of 950,000 Haikwan taels, for which the salt revenue is responsible.
- With regard to the railway loans, the position is no better than it was at the end of 1929, and no serious effort is beng made by the Government to deal with this problem. Protests on the subject of defaults follow the regular routine of being referred by the Waichiaopu to the Ministry of Railways, who invariably reply to the effect that the general readjustment of railway loans is being considered, and that, as soon as a satisfactory plan has been evolved, the creditors will be notified. The only railway loan that can be said to be running according to schedule is the 5 per cent. Imperial Railway Loan of 1899, which is secured on the Peking-Mukden Railway. This line was not affected by the civil war, and its earnings during the year were ample to meet all its obligations and leave a large surplus. It is some small satisfaction, therefore, to record that, in addition to maintaining the service of the original loan of 1899, payments were resumed on the Double Track Loan, but this was only achieved by constant pressure on the part of His Majesty's Minister, and the bulk of the surplus earnings, as mentioned elsewhere in this report, have been used for extraneous purposes, regardless of the prior obligations to which this revenue has been pledged. The Railway Administration, for instance, flatly refuse to pay anything on account of the Shanghai-Fengching Railway Loan, which has been in default for years, so that the Loan Agreement in respect to the important question of security is practically a dead letter. With the railway in a flourishing state, it might at least have been expected that something would be done towards paying their outstanding accounts for rolling-stock, but no attempt has been made to settle the debt contracted in 1922 with Messrs. J. Whittall and Co. (Limited) (who were forced into liquidation through its non-payment), which now amounts to more than £700,000.
- 315. British trade has been heavily hit by the load of unpaid debts for railway material, which has had the effect of crippling the activities of some of the leading British merchants in China, and may yet force others besides Messrs. Whittall and Co. into liquidation. If these debts were ordinary trade risks, nothing could be said about it, but, considering that hundreds of millions of dollars have been raised during the last few years by domestic loans, it is impossible to believe that the Chinese Government, if they were genuinely desirous of honouring their obligations, could not have done something to assist these long-suffering creditors. Despite the fact, however, that many of the railways have from time to time been earning, and are now earning, substantial revenues, nothing stirs the Chinese Government to a sense of the injustice of the position. Debts of this nature should rank with salaries and wages in priority to all other railway obligations, and, as the rolling-stock and materials supplied by British creditors have actually been in use for years past, and earning money for the respective railways, it is nothing short of a scandal that the Chinese Government fail to make any provision for their liquidation.

Customs.

316. The total revenue collected by the Maritime Customs in 1930 amounted, in round figures, to 180,570,000 Haikwan taels, an increase of 27,810,000 Haikwan taels over the previous year. The greater part of this

increase came from Shanghai, the collections at that port having exceeded those of 1929 by 17,200,000 Haikwan taels. This satisfactory result was chiefly due to the introduction of the new gold unit referred to in last year's report, and does not imply any improvement in the trade of the country. All the foreign loan and indemnity obligations secured on the customs revenue, including the service of the Reorganisation Loan, were met in full, but, owing to the heavy depreciation of silver during the year, the silver cost of these obligations exceeded that in 1929 by more than 26 million Shanghai taels.

317. The service of all domestic loans and Treasury notes secured on the customs revenue has also been met or provided for in full.

Debt Consolidation.

[6096]

318. Since China became a republic each successive Chinese Government has shown itself better at recognising debts than paying them, and the present Government has done nothing to shatter this tradition. When tariff autonomy became a fait accompli they evidently felt that something was expected of them, and it will be remembered that on the introduction of the new tariff the sum of 5 million dollars per annum was allocated out of the increased customs revenue for the consolidation of internal and external obligations. Even this comparatively insignificant amount, however, was not voted spontaneously, but was due to pressure on the part of the Japanese Government, who have all along been particularly active in keeping the National Government up to the mark on the question of debt consolidation. In their Tariff Treaty of the 6th May, a special annex was included on the subject requesting that a conference of creditors should be called at an early date, to which the Chinese Government formally replied that it was their intention to call such a conference on or before the 1st Oc. ober. The civil war, however, intervened to make that date impracticable, and the Nanking Government were only too ready to take advantage of this to postpone the conference indefinitely, but the Japanese insisted on it being held, and the Minister of Finance was reluctantly persuaded to fix the date for the 15th November.

319. Japan's persistent attitude over this question is somewhat of a mystery, but it is thought that their anxiety to force debt consolidation—apparently at any price—is due to reasons of domestic policy, and they are certainly in a better position to make concessions than other creditors because the greater portion of their debts are practically Government debts. The Nishihara Loans, for instance, which the Japanese insist must be recognised, but the Chinese are equally insistent in excluding, were long ago taken over by the Japanese Government. These much discussed loans form a large part of the Japanese claim, and it is believed that they are prepared to make heavy sacrifices to secure their recognition by the Chinese Government. So anxious were the Japanese Government to come to terms with the Chinese over this debt question that they appointed the Japanese Chargé d'Affaires at Nanking as the official representative of Japanese creditors, and it was credibly rumoured that Mr. Shigemitsu was prepared to offer very favourable terms if China would come to a prior settlement with Japan. It was at any rate a fact that the way to the conference was paved with conversations and discussions between Mr. Shigemitsu and Mr. Scong, and both Chinese and Japanese schemes were drawn up outlining their respective ideas as to the consolidation of China's unsecured debts. These proceedings, however, were kept strictly secret, and some dissatisfaction was felt by the rest of the creditors at the hole and corner methods employed, the shortness and irregularity of the invitation to the conference, and the entire absence of information as to the proposals the Government intended to make. Nevertheless, the day of the conference found representatives of all the creditor Legations assembled at Nanking, waiting in somewhat paradoxical fashion for the debtor to pronounce If they expected a cut and dried scheme of debt consolidation to be put before them, they were doomed to disappointment. All the leading members of the Chinese Government were present at the conference, and a memorandum entitled "Tentative plan without commitment" was presented by the Commission for Readjustment of Domestic and Foreign Loans of which Wang Chung Hui had just been selected chairman and Marshal

Chang Hsueh-liang one of the members. This so-called tentative plan did not contain a single figure, and bore still less evidence of any genuine "will to pay. On the contrary, it was obviously the bare framework of a scheme the main object of which appeared to be to limit the amount for which the Chinese Government would be prepared to issue bonds in settlement of China's unsecured indebtedness. The idea in a nutshell was to restrict payments to two sources, viz., the customs revenue and the railway revenues, payments from the former to terminate in 1960 and to be "subject to priority of a reserved charge to be used for purposes of rehabilitation," but no amounts were specified. The customs revenue, however, is heavily pledged for years to come, and it is worthy of note that a new loan of 50 million dollars secured on the increased customs revenue was rushed through almost whilst the conference was sitting. It seems impossible for the Government to keep their hands off this revenue, and reference has already been made to a further loan of 80 million dollars, which, at the time of writing, has just been placed on the market. The prospects of a practical scheme of debt consolidation being evolved with the surplus customs revenue as security, are therefore even more desperate than they were at the time of the conference.

- 320. British interests are, of course, chiefly concerned with the railway loans and debts, and this was vaguely dealt with in the tentative plan, the suggestion being that railway debts that could reasonably be carried by the respective railways should be paid out of railway earnings. This was accompanied by a valuable concession—in principle at any rate—that a portion of the sums paid from customs revenue (for debt consolidation) would be used in payment of these debts. Unfortunately, there was a further stipulation that railway debts would only be paid "after measures of rehabilitation and restoration have been taken," and this might well prevent any revenue from ever finding its way to the creditors.
- 321. It is difficult to resist the conclusion that the Chinese Government, in calling the conference at the instigation of the Japanese, were animated not so much by a desire to effect a just and honourable settlement with their creditors as to seize the opportunity to make a hard and fast bargain, restricting the sources of payment to the customs surplus (which has already been bled white by domestic loans), and the railway surplus revenues (if any) over which they have at present little or no control.
- 322. The understanding at the close of the conference was that the Chinese Government would call another meeting at some future date, when the Legations concerned would have had time to consider their views and prepare their lists of debts. The further heavy slump in silver, however, which has since occurred, has upset all ideas of debt consolidation and the probabilities are that no further meeting will be called.

British Claims.

323. A list of British claims against the Chinese Government for loans and obligations in default as at the 31st December, 1930, has nevertheless been prepared, and the following are the totals in round figures of principal and interest outstanding in the various categories:—

Railway loans and advances (exclusive of the international loans, viz., Hukuang and Tientsin-Pukow): £2,260,000 and 2,450,000 Chinese dollars.

Railway debts for material: £1,138,000 and 11,520,000 Chinese dollars. Ministry of Finance loans and advances (chiefly Vickers and Marconi loans and excluding the international Anglo-French Loan): £5,815,000 and 2,730,000 Chinese dollars.

Ministry of Communications debts: £26,000 and 14,000 Chinese dollars. Ministry of Finance debts: £84,000 and 6,970,000 Chinese dollars.

324. Owing to the constant fluctuations of exchange the sterling totals have not been converted into dollars, and are therefore quoted separately. The above figures show that the grand total of principal and interest outstanding of all British loans and obligations as at the 31st December, 1930, amounts to £9,320,000, and 23,680,000 Chinese dollars.

Chinese Government's Annual Report and Budget.

325. Following up last year's precedent, Mr. T. V. Soong has recently (on the 1st March, 1931) published the second annual report on the national finances of China for the year ended the 30th June, 1930. This report is fully on a par with its predecessor in clarity and outspokenness and indicates an honest desire on Mr. Soong's part to face the facts, but it must be confessed that the results as disclosed in the balance-sheet are not encouraging. Handicapped as he was by what he describes as "the most serious civil war which it (the Government) has had to confront since its inception," it was not surprising that there should have been a deficit of upwards of 100 million dollars. Mr. Soong, however, states that "given the absence of unforeseen events it is possible that by united exertions budgetary equilibrium may be attained at same time during the fiscal year ending the 30th June, 1932," but in view of his own admission that the deficit during the six months ending the 31st December, 1930, as a result of the civil war, will be even greater, it is difficult to have much confidence in this optimistic forecast.

326. It is worthy of note that of the total revenue of 483,700,000 dollars, more than 80 per cent., or 397 million dollars, was produced by the foreign-controlled customs and partially foreign-controlled Salt Gabelle, the receipts from the latter having jumped stupendously from 30 million dollars in 1928–29 to 122 millions in 1929–30. Domestic borrowings during the year amounted to 100 million dollars.

327. On the expenditure side of the account the outstanding feature is the cost of the military establishments, amounting to more than 245 million dollars, which represents half of the whole expenditure for the year and almost five times that of civil establishments. The next heaviest burden on the exchequer is the amount required for the loan services and indemnity payments, which came to 200 million dollars.

328. Mr. Soong does not confine himself to the period ending the 30th June, but makes several interesting statements on matters of more recent date. He skates lightly over the question of debt settlement, realising no doubt that the ice is very thin. After a brief reference to the November Conference and "the memorandum containing broad general principles," which was submitted by the Commission for Readjustment of Domestic and Foreign Loans, he says that "every effort is being made to overcome the numerous and complicated obstacles to an early settlement, so that confidence in the national credit may be restored and the way paved for introduction of foreign capital." Nevertheless, within a few days of this pronouncement a new loan of 80 million dollars, secured on the increased customs revenue, was announced regardless of the "broad general principles" of the memorandum, of which the essential feature was that the customs surplus up to 1960 should be used as a basis for a debt consolidation scheme.

329. While recognising that foreign capital is required for the rehabilitation of the country, Mr. Soong has no illusions as to the terms on which it is likely to be forthcoming. He frankly states that "foreign lenders will not discuss loans to China unless China has balanced its budget, or has adopted, and is carrying into effect, a programme of readjustment which will result in stabilising the finances within a reasonable time."

330. Rumours as to "the loan projects that are now receiving popular attention" are lightly touched upon as being doubtful of realisation, and this presumably refers to the tentative proposals for a silver loan to China which have been appearing in the American press for some time past, emanating from Senator Key Pittman and Senator Tasker L. Oddie, both of the great silver-producing State of Nevada. These Senators went so far as to put a resolution before the American Senate proposing that a huge silver loan should be advanced to China without security and at a low rate of interest. This resolution was not acted upon, however, even by the Senate Foreign Relations Committee, and it would seem that the proposed loan was merely a desperate attempt on the part of the silver interests in America to dispose of their surplus stocks. China is not in the habit of refusing loans, especially when they are offered without security, but

the methods of finance suggested in the present case are so visionary that it seems unlikely that they will lead to any practical result.

331. Mr. Soong had some interesting remarks to make on the subject of li-kin abolition, which, he claims, "has met with an astonishing degree of success, exceeding all expectations," and he affirms that "the lost of revenue itself is estimated at over 80 million dollars, but the direct saving to the people must be a least 160 million dollars, the difference representing wasteful expenses and the various forms of irregularities which honeycombed the system." The conclusion of his report bodly states the case for the limitation of military expenditure, the funding of short-term loans, and the attainment of budgetary equilibrium. At the same time he realises that something more is demanded of the Government than mere budget equilibrium and describes this desideratum as what is "vaguely expressed in the popular mind by the word 'reconstruction.'" Finally, he sums up the situation as follows:—

"Surely a case has been made for discarding the haphazard, unrelated, and clashing programme of the various branches of the Government and the creation of a really effective planning organisation which would guide the productive forces of the country, co-ordinate the activities of the Ministries, and rigidly map out the essential ends which, for a given course of years, each of the different components is obliged to pursue. With such co-ordinated and purposeful activity within the Government, whereby it is made a unified and effective instrument to serve the nation, the financial resources available within the country itself for constructive development will prove to be greater than is ordinarily realised."

Whether these counsels of perfection are assimilated in the proper quarters or not, Mr. Soong must be given due credit for being the first Minister of Finance in China who has had the courage to tell home truths in plain language and to make constructive efforts to put the finances of the Government on a sound basis.

V.—TRADE.

(a) General.

332. The total value in Haikwan taels of China's foreign trade in 1930 was, in round figures, 2,204 millions, a falling off of 77 millions, in comparison with 1929, for although imports increased by 44 millions the decrease in exports amounted to 121 millions. As compared with 1929, the balance of trade against China increased from 250 millions to 414 millions. Great Britain's share of the trade decreased in value by about 11 millions in the case of imports and 12 millions in exports, and as regards the import trade she fell to the fourth place in the list, the first three positions being taken by Japan, the United States of America and British India. Measured by gold standards, China's total trade fell from £302 million to £208 million on the basis of the average value of the Haikwan tael in 1929 and 1930 respectively. The above figures have been quoted in Haikwan taels, this unit having still been retained by the customs for statistical purposes, although duties are calculated in "gold units" equivalent to 0.40 gold dollars.

333. As regards the export trade, it might naturally have been expected that the lower rates of exchange would have afforded an excellent opportunity of finding a market for Chinese produce, but whatever advantage may have been derived from this factor was more than offset by the industrial depression existing in Europe and the United States of America, which seriously affected the demand for practically all the staple products exported from this country, and was particularly apparent in the case of the silk and bean trades, which occupy such important places in the list of China's exports. In addition to this absence of demand in the consuming centres, China's export trade had to contend with the difficulties arising from unsettled political conditions, insecurity and brigandage in many of the producing districts, inadequate means of transportation, and heavy taxation en route to the ports of shipment.

334. Against this serious decline in the value of China's exports, the customs figures show a considerable advance in the silver value of her import trade, but the increase is mainly to be found in the case of food-stuffs and raw materials, and

not in manufactured goods. Poor crops in certain districts, and, to a still greater extent, the lack of adequate means of internal communication, necessitated the importation of large quantities of rice, wheat and flour, whilst imports of raw cotton to supplement native supplies were also unusually heavy. The latter circumstance is the chief explanation for the fact that the total value of imports from British India last year increased by nearly 150 per cent. over the 1929 figures and placed her well ahead of Great Britain in the order of precedence.

335. It must, I think, be recognised that, owing to a variety of circumstances, the nature of China's import trade has been steadily changing during the past few years, the proportion represented by food-stuffs and raw or partially-manufactured materials showing a marked increase, whilst there has been a corresponding decline in the share taken by manufactured goods, other than certain special types of products, such as machinery and motor vehicles. As regards food-stuffs, the necessity for importing enormous quantities of rice and other cereals into an agricultural country such as China has been due mainly to disturbed conditions in many of the producing districts and to transportation difficulties, whilst in the case of raw materials, although China's industrial development has been retarded by political insecurity, it is undoubtedly making steady progress and requires larger quantities of such materials as are not procurable locally.

336. On the other hand, the enormous advance in the cost in local currency of all imported goods, owing to the depreciation in the value of silver, has tended to place them beyond the means of all but a comparatively small section of the population, and the buying capacity of the people has in any case been seriously affected by a long succession of civil wars and disturbances. The reduction in demand resulting from prices being driven up to a figure beyond the means of the consumer has had a serious effect even on the sales of commodities in universal use, such as kerosene, and is naturally still more noticeable in the case of goods not coming under the description of common necessities of existence. A further result has been to make price, rather than quality, the primary consideration, and so to increase the difficulty of finding a market for British goods in competition with cheaper products of native or foreign origin.

337. From the point of view of the importer, the commercial situation in China during 1930 was, in fact, entirely dominated by the sensational fall in the value of silver, rates for the Shanghai tael dropping from 2s. $0\frac{3}{4}d$. to 1s. $4\frac{7}{8}d$., and as local prices were slow to adjust themselves to so marked a depreciation, merchants experienced great difficulty in enforcing the prompt fulfilment of existing contracts and found it almost impossible to secure orders for future delivery.

338. The effect was, unfortunately, particularly noticeable in the case of cotton piece-goods, which still constitute the most important item in British trade with China, and whilst detailed figures are not yet available there can be little doubt that the customs returns will show a further decline both in the volume of British imports into this country and in our proportion of the trade. In one respect only can the situation be described as at all satisfactory. The fact that new business has been on so restricted a scale has led to a considerable depletion of stocks, both in the main distributing ports and in the consuming districts, and with any improvement in exchange rates or even some sign of stability there is reason to hope for the development of a better demand.

339. The machinery trade showed much greater signs of activity during the past twelve months, and although the number of important contracts actually placed was not very large firms interested in the engineering business received many enquiries for mills, electrical installations and industrial plant of every description. The carrying out of most of these more ambitious schemes has been held up either on account of the high cost in local currency, owing to unfavourable exchange rates, or to difficulties in arranging satisfactory terms of payment, but in small machinery and engineering supplies business was fairly good. The indications are that it is in the machinery trade that British manufacturers are likely to find the best prospects of finding a market for their products in China. As stated in a previous paragraph, the industrial development of China is making slow, but steady, progress, and this tendency has been accelerated by the rising

cost of imported goods caused by the fall in the value of silver, and more recently by a substantial increase in the import duties on certain commodities. In some lines of business the products of native factories are already driving even the cheapest foreign goods of similar type off the market, and if political conditions continue to offer some prospect of stability, a great expansion of local industries, accompanied by an increased demand for machinery and engineering plant generally, must inevitably take place.

340. To return to the year 1930, however, it must be admitted that, for foreign trade generally, and for Great Britain in particular, conditions in China were extremely unsatisfactory, and that prospects for the immediate future are hardly more favourable.

(b) The British Economic Mission.

341. The British Economic Mission to the Far East was appointed by the Secretary of State for Foreign Affairs and the President of the Board of Trade on the 18th August, 1930, to enquire into the present condition of British trade with China and Japan, and to report what action should be taken to develop and increase that trade. The mission, under the chairmanship of Sir Ernest Thompson, J.P., was accompanied by a cotton mission representing the Lancashire cotton trade. It left London on the 19th September, 1930, and arrived at Tokyo on the 30th October, 1930. After spending four weeks in Japan, the mission arrived at Shanghai on the 30th November, 1930. In China, visits were made to Nanking, Shanghai, Tientsin, Peking, Harbin, Mukden, Dairen, Tsingtao and Canton. A party of the mission also visited Hankow. Valuable assistance in the shape of the preparation of a considerable amount of data dealing with various aspects of British trade with China, and of replies to questionnaires, was furnished by the British Chambers of Commerce in China. The mission was presented to the President of the Chinese Republic at Nanking by Sir Miles Lampson in the first week of December, immediately after its arrival in China, and its members were received and entertained by several of the leading personalities of the Chinese Government, including the Ministers of Foreign Affairs, Industry and Commerce, and Railways. It was expected that the mission's report would be ready for publication shortly after their return to England early in April 1931.

V1.—TAXATION AND TARIFF.

Taxation.

342. The much-heralded abolition of li-kin, and all other internal taxation ejusdem generis, was finally decided to take effect from the 1st January, 1931. This decision was the immediate result of the conference of the fourth plenary session of the Central Executive Committee held at Nanking in November last. It was announced in a circular telegram issued by the Ministry of Finance, dated the 15th December, and in a message from the President, dated the 27th December, giving the Government's reasons for the step, and expressing its determination to carry it through without further delay, in spite of the opposition of the provincial authorities, which was already being voiced from all quarters. Li-kin abolition had previously, by mandate of the 17th January, 1930, been fixed for the 10th October, but owing to civil war conditions and consequent lack of control by the Central Government over the provinces, it had, by a further mandate of the 6th October, been again postponed to the end of the year. While the intentions of the National Government in their endeavours to assert once and for all the principle of the single tax on all goods, whether imported or produced within the country itself, were no doubt sincere, it is to be feared that their hold over the provinces, particularly the outlying and frontier provinces, is too insecure to make their order binding. It does not appear, moreover, that the proposed new consolidated forms of taxation to take the place of li-kin have been sufficiently thought out, or discussed with the various provincial authorities, or that effective preparations have been made to remit appropriate subsidies to the various provinces to compensate them for any deficits in their budgets arising from the abolition of li-kin. This state of affairs was partly due to the state of

civil war; in fact, a *li-kin* abolition conference, called at Shanghai in June, had to be postponed owing to lack of response to the invitations issued by the Government, and in the end it was only attended by delegates of the provinces immediately under the control of Nanking. In short, there is reason to fear that the new order may only mean the perpetuation of the old vicious, unsystematic lax levies under changed names, and that the difficulties of the importer of foreign goods, already faced with higher tariff duties, will be proportionately increased. Be this as it may, there is no doubt that a genuine attempt was made to bring about the abolition of the *li-kin* collectorates throughout a considerable part of the country on the first day of this year, and that in the provinces immediately under the sway of Nanking, this attempt was in a considerable measure successful.

343. Simultaneously with the abolition of li-kin, the Central Government also abolished such other forms of internal taxation as inward and outward transit dues, parcel post tax, coast trade duties, and extra-50 li customs duties. The abolition of coast trade duty (i.e., half the export duty) was a reform strongly advocated at the Special Tariff Conference of 1925–26, and the removal of this form of taxation gives considerable impetus to the free movement of cargo between Chinese ports. It is unfortunate that this step is not to be accompanied, as might be expected, by the simultaneous removal of the full export duty on native goods carried from one Chinese port to another. The removal of both the full and the half export duty on such cargo formed part of the abortive proposals submitted by the Chinese delegation at the Special Tariff Conference, subject to certain precautions designed to prevent the fraudulent shipment abroad duty-free of goods liable to export duty. Presumably, the loss of revenue involved in the abolition of the full as well as the half duty on native cargo carried between Chinese ports was too large to be contemplated for the time being, though it seems illogical to remove, at any rate in theory, all taxation on goods in transit overland, while an export tax is still collected on cargo transported by steamer from one Chinese port to another.

344. The abolition of the treaty-made transit pass system is a natural corollary of the abolition of *li-kin*; it is, however, too early yet to say whether the latter reform will be sufficiently comprehensive to justify the removal of this privilege, particularly as regards export cargo. In the long run, however, it can only be left to the common sense of the Chinese themselves and the tightening of the Central Government's hold over the provinces, to put an end to the strangle-hold which the many purely local and uneconomic tax levies still have on the trade of the country.

The Minister of Finance assessed the loss of annual revenue from li-kin proper at 80 million dollars, and that from native customs, coast trade, and other duties on goods in transit at another 19 millions, making roughly 100 millions in all. The taxes designed to make good this deficiency were mainly of three classes. The first is a consolidated tax (or excise duty) on certain goods, such as cotton yarn, matches and cement, similar to the excise duty already collected through the customs machinery on oil and cigarettes. The second is a consumption tax, or "special" tax (really also an excise duty), on a number of other classes of goods, mainly goods of native production, on the basis of certain regulations issued in 1928 (see paragraph 356 of last year's report), which were designed to cover nineteen different commodities of wide range. The amount of the taxes to be collected from these goods was originally to be left to the provinces themselves to decide, but now a schedule of these duties is under the consideration of the Ministry of Finance, which intends to collect them for the national account on a uniform scale in every province (in the meantime, the provincial authorities are being allowed to collect some, at any rate, of these taxes at the old li-kin rates). While the consolidated taxes on yarn, cement and matches have already been fixed and are being collected, the "special" taxes on other goods are still to be decided. The underlying principle of these forms of taxation is the collection by the agents of the Central Government of a single tax on specified goods of native provenance at the place of production or manufacture, in place of a transit tax, of the nature of *li-kin*, which was collected by the provinces themselves many times and on all goods. It is still open to question whether, in the case of goods liable to these consolidated or consumption taxes, the Government intends to discriminate against imported goods by making them pay the full amount of such taxes in addition to enhanced import duties. In theory, no doubt, they would prefer these excise taxes to be collected, as in the case of oil and cigarettes, together with the import duty, by the customs at the moment of import, but it is doubtful whether in all cases this will be possible in practice. A case in point is the recent collection, through the machinery of that Maritime Customs Administration at Tientsin prior to the release of cargo, of a surtax on imported flour (there is no import duty on flour), which in theory corresponds to an excise tax on native-milled flour. While the collection of such extra-tariff taxation by the customs may be open to objection in principle, there would, in the new situation created by the tariff autonomy treaties, appear to be no good answer to the Chinese contention that such collection is purely a matter of internal organisation and collaboration between two tax Departments of the Government. It is, in fact, the recently declared intention of the Minister of Finance that, with the abolition of li-kin, excise and consumption tax on imported foreign goods, or goods exported abroad, shall be collected by the maritime customs at the time of importation or exportation, as had already been the practice in regard to oil and cigarettes; out of the revenues so obtained some sort of subsidy will be paid to the provincial Governments. The third new form of taxation is to be a business tax, or graduated tax on the capital (or turnover) of business concerns. It was originally intended that this form of taxation should be levied by the provinces themselves, each framing its own regulations and scale of taxation in accordance with certain guiding principles laid down by the Executive Yuan of the Central Government, and that the provinces should recoup themselves mainly out of this tax for the loss of their li-kin revenues. difficulties of instituting any such type of taxation in a country like China, where the preparation of anything in the nature of income tax forms has hitherto been unheard of, does not appear to have been properly considered by the Ministry of Finance, and, so far, the only result has been that certain provinces, e.g., Hupeh, have issued regulations which are discriminatory in form and would impose impossible handicaps on certain classes of business, and which do not even conform to the principles laid down by the Ministry itself; moreover, they are enforceable by arbitrary executive action rather than by any due process While these regulations are stated to apply to foreign as well as to Chinese firms, no serious effort has yet been made to enforce them against British concerns, and Sir Miles Lampson, in pointing out the anomalies, and even absurdities, contained in them, to the members of the Government principally concerned, has adopted the standpoint that the application of any such taxation to firms having extra-territorial privileges should properly await the outcome of the extra-territoriality negotiations now proceeding. The result of the existing confusion in regard to this tax, which is also meeting with considerable popular opposition, will probably be that the Government will itself have to frame the regulations under which it is enforced. The separation of national and provincial revenues under all these new schemes of taxation is certain to prove an extremely thorny task, and it will be difficult for the Ministry of Finance to achieve even the semblance of a unified financial control. In some of the frontier provinces, such as Yunnan and Szechuen, the decrees of the Central Government in matters of finance are frankly disregarded; in others, such as the Manchurian provinces and Hopeh, which are under the control of Marshal Chang Hsueh-liang, stability can at present only be achieved by a complicated process of bargaining between the central and local authorities, while all the tax officials, though nominally under the orders of Nanking, are actually nominated by, and owe allegiance to, the Mukden faction.

346. Previous to the abolition of li-kin at the end of the year, civil war conditions through the greater part of the country had given rise to all sorts of local and military levies, collected even from goods under transit pass, though there was, generally speaking, no question of discrimination against foreign goods. In certain provinces, such as Yunnan and Szechven, many forms of taxation not countenanced by the Ministry of Finance have flourished. At Chungking a 2½ per cent. surtax is still being collected on all imports and exports, as well as a 2 per cent. road-construction surtax; in Yunnan, a special import tax was collected during the year, which, in many cases, exceeded the original import duty; this latter tax was, however, abolished at the end of October. Other

provinces immediately under the control of Nanking were "preparing for" the abolition of Nanking by instituting various forms of consumption taxes, many of which appeared to conflict with the assurances given to us in annex 3 of the Sino-British tariff treaty of December 1928.

- In many provinces, such as Hopeh, in recent years, the li-kin, which vas originally a transit tax on all goods, has become more and more a "consolidated" tax ("t'ung shui") on certain specified classes of goods, such as skins, furs, wool, strawbraid, "cotton and dried fruits." These "consolidated" taxes are now, in turn, gradually coming to be known as "consumption" taxes, but in reality they are, in many cases, almost indistinguishable from the original li-kin. At the smaller treaty ports, where there are no concession or settlement areas, where foreign goods are immune from taxation not authorised by treaty or special arrangement, the only British firms importing goods for their own account on any large scale are the big distributing companies, which have made their own special taxation arrangements with the Central Government (in regard, at any rate, to most of the commodities they sell)-arrangements which are, generally speaking, recognised by the provincial authorities. The collection of these irregular forms of taxation tends, therefore, more and more to fall on the native dealer in imported goods. As is inevitable in the changing order of things, foreign merchants in China are, in fact, becoming increasingly disposed to leave their taxation difficulties to their Chinese friends to settle for them. The interests of the Chinese merchants are frequently bound up with, or even identical with, those of their foreign colleagues and rivals, and they are invariably more adept at bargaining with the tax collectors.
- 348. The order for the abolition of *li-kin* resulted in the closing of the notorious Peking Octroi bureaux, against which there has always been much popular agitation. This tax, which was collected indiscriminately on all merchandise passing the city gates, was originally established to provide certain expenses of the court under the Manchu dynasty, and was later on appropriated, in part at any rate, for the upkeep of the presidential establishment. Its removal provided a timely relief to the declining trade of the old capital.
- 349. Attemps to levy contributions to forced loans from British subjects were resisted during the year at Chungking and Hankow.
- The Nanking Government have, of recent years, shown themselves unwilling to grant what is known as "privileged factory treatment" to the machine-made products of industries in this country, established with foreign capital, or controlled by foreign firms. This privilege, which is of long standing, though not based on any treaty right, and which was formerly granted to all factories, on the completion of certain formalities, whether established with foreign capital or not, entitles the products of the factories to which it is granted to the payment of a single export duty (nominally 5 per cent.) at the first customs barrier passed, and to immunity thereafter from payment of any coast trade duty, or any other form of internal taxation whatsoever. Privileged factory goods exported abroad are, moreover, totally exempt from duty. The advantage of the former privilege is now smaller owing to the abolition of the coast trade duty. The recent reluctance of the Government to grant these privileges to so-called "foreign" factories is inspired by the desire to compel the firms owning them, which are in most cases sheltered by extra-territorial privileges, to register and pay registration fees under Chinese company legislation, and generally to render themselves liable to Chinese taxation, factory laws, &c. The principal members of the Government are, however, not slow to recognise the shortsightedness of discouraging the investment of foreign capital in Chinese industries. The question will probably only find a solution as part of the extra-territoriality settlement, but in the meantime it seems likely that many foreign firms operating factories in China will register under Chinese law in order to obtain privileged treatment.

Tariff.

351. Apart from the institution of the gold unit system of duty payment, explained in paragraph 349 of last year's report, no radical changes were made during 1930 in the import tariff introduced on the 1st February, 1929. Since

March 1930 the tariff has been published in gold units, and the specific duty rates are expressed in this unit in the revised import tariff recently promulgated on the 29th December, 1930. This tariff is to be effective from the 1st January, 1931, and was introduced without previous notice. In the new tariff numerous changes have been made in the classification of goods and in the specific duty rates. The rate on woollen yarn and manufactures, artificial silk yarn, sugar soda ash, wines, cigarettes and tobacco and other luxuries have been considerably raised, while the duties on certain classes of machinery essential to Chinese industries have been lowered. It is confidently expected by the Chinese National Tariff Commission, which framed it, that the new tariff will produce a considerable increase of revenue; it is open to question, however, whether, in many instances, the duties have not been raised to a figure where the revenues will be subject to the law of diminishing returns. The enhanced duties on certain classes of woollen manufactures, which gave evidence of miscalculation on the part of the framers of the tariff, have been made the subject of representations by the foreign interested firms to the competent departments of the Chinese Government, with the result that these goods are to be allowed to pay an optional ad valorem duty in place of the new specific duty rates. It remains to be seen whether the Government will be prepared to revise any of the other duties against which criticisms have been freely levelled.

- 352. Representations were made by this Legation to the Chinese Government during the year with a view to obtaining a reduction, or the removal, of the import duty on linen cloth and linen union piece-goods, imported chiefly from the United Kingdom or the North of Ireland, for embroidering in Chinese factories and subsequent re-export, principally to the United States of America. These representations were, however, not acceded to by the National Government.
- 353. China's right to complete tariff autonomy was further recognised in the Sino-Japanese tariff treaty signed in May 1930. This treaty introduced the principle of tariff reciprocity, as in it China agreed to maintain the existing rates of import duty on certain kinds of cotton goods and sea products for three years, and on certain miscellaneous goods for one year, while Japan agreed to maintain for three years her present rates of duty on Chinese grass cloth, and to reduce by 30 per cent. ad valorem the import duties on certain kinds of luxuries such as silk piece-goods and embroidered tissues. The goods in question were all of a kind in which Japan and China were peculiarly interested.
- 354. It is said that the National Government shortly intends to raise the export duties to an effective 5 per cent. The tariff on exports has remained virtually unchanged since it was promulgated in 1858; it is nominally on a 5 per cent. basis, but many of the specific duties are actually much lower, being only 1 or 2 per cent. of the value of the goods. Since February 1929 a surtax of half as much again has, however, been collected by the customs. It is presumed that if the specific duty rates are raised to an effective 5 per cent. (or any approximate rate), this surtax will be abolished.

VII.—MARITIME CUSTOMS ADMINISTRATION.

355. The history of the Chinese Maritime Customs Administration during the past year has been marked by two questions of outstanding importance: the seizure of the Tientsin Customs-House by the Shansi faction in June and the negotiation of an agreement on the Hong Kong customs question between the Inspector-General of Customs and the Government of Hong Kong. This agreement, however, when finally submitted to the Central Executive Committee of the National Government, proved abortive owing to the opposition of the Canton faction, though fully approved by the Minister of Finance and other members of the Government.

(1) Seizure of Customs-House at Tientsin by Yen.

356. The seizure of the Tientsin Customs-House by Mr. B. Lenox-Simpson, under the orders of the rebel Marshal Yen Hsi-shan, arose out of the desire of the Shansi authorities to prevent the Tientsin customs revenues, over and above

the proceeds of the original 5 per cent. tariff which are devoted to the foreign loan payments (or, in other words, the so-called "additional" revenues), being remitted to Shanghai to swell the coffers of the Nanking Government, against which he had taken up arms. The latter refused to countenance any arrangement providing for the detention, even temporarily and in "neutral" banks under a tuarantee that they would not be touched by either side pending the issue of the struggle, of the Tientsin "additional" customs revenues, declaring that such a step would impair the integrity of the customs and, by creating a dangerous precedent, would shatter China's credit at home and abroad. This uncompromising attitude on the part of the Nanking Government in face of a situation in which they were powerless to bring any forcible pressure to bear, eventually led the Shansi leader to instruct Mr. Lenox Simpson (the well-known writer "Putnam Weale"), a British subject who had previously been acting the part of a publicity agent of the Northern party as editor of the "Peking Leader," to seize the customs-house and eject the commissioner, Mr. Hayley-Bell. This he did on the 16th June. Similar action was threatened by the Northerners at Chefoo, Tsingtao and Hankow, though it actually never took place, as the Shansi faction were never strong enough to consummate it at these ports. Seeing that it was neither politic nor practical in the circumstances to interfere with the functioning of the new irregular but *de facto* customs organisation set up by Mr. Simpson, British and other foreign nationals were advised by their authorities to pay the customs duties to it in the normal way. The majority of importers and exporters being Chinese firms, it was also considered impracticable to establish any system of consular collection of duties payable by foreign firms or acceptance of guarantees for payment thereof. The whole of the proper customs staff were withdrawn from the customs-house under orders from Nanking, and the customs-house was declared "closed" from the 20th June. Mr. Simpson, however, with considerable ability, managed to carry on the work of dutycollection with an improvised staff consisting largely of former (and in some cases dismissed) customs servants. The present customs-house at Tientsin is situated in the French concession, but the French authorities took the line that they were not called upon to interfere except in the case of a breach of the peace, which did not occur, as Mr. Hayley-Bell left the building without resistance when called upon by Mr. Simpson to do so. Mr. Bell had all along opposed any suggestion of a compromise and had made no secret of his views to the local Shansi officials. The National Government pressed with the utmost insistence for the prosecution of Mr. Simpson under article 75 of the Order in Council of 1925 and for his deportation, but His Majesty's Government, after full consideration of all the circumstances, decided that such a course was inexpedient. Considerable embarrassment was for a time caused to the trade of Tientsin by the retaliatory action of the Nanking Government in collecting at Shanghai and other ports all duties on coast trade cargo and transshipment cargo from abroad properly leviable at Tientsin, which meant double payment of duty. The coastal trade being almost entirely in the hands of native shippers, it was not considered justifiable to resist these measures by any attempt to force the hands of the customs, who were merely carrying out the orders of Nanking, though, if persisted in for a considerable period, the effect on coastal shipping, which was chiefly British and Japanese, was likely to be serious. Through cargo for Tientsin in vessels calling at Shanghai was not interfered with, though such action was threatened. On the 1st July the diplomatic representatives in Peking forwarded two communications to the Chinese authorities, one to Marshal Yen Hsi-shan, disapproving of his action in disorganising the Customs Administration, the other to the Nanking Government, protesting against their retaliatory action in ordering the collection of Tientsin duties at Shanghai and other ports in defiance of article 25 of the Sino-British (Tientsin) Treaty of 1858. Each of these notes communicated a copy to the other. In the meantime every effort was being made by the British and Japanese representatives to assist in bringing the two sides to a suitable compromise, though Sir Miles Lampson made it clear to all concerned that he could not be drawn into any discussion of detail or bargaining between the two parties, or take any action outside the rôle of a friendly intermediary. To facilitate a compromise solution, the Inspector-General of Customs instructed Mr. Hayley-Bell to hand over the duties of commissioner, which were, of course, in abeyance, to Mr. Grierson, the previous deputy-commissioner, and himself to proceed on leave. It was, however, difficult

for those working in the interests of a compromise to make the terms offered by the Minister of Finance after the seizure of the customs-house known to Marshal Yen Hsi-shan, who was then at the Shansi capital, Taiyuanfu, fully occupied with the prosecution of the civil war. Possibly owing to Mr. Simpson's influence, in his own personal interests, all efforts to effect a compromise at this late hour, whether by negotiation between the officers of the maritime custom proper remaining in Tientsin, or by the communication to Marshal Yen through the British and Japanese Legations of proposals acceptable to Nanking, proved unsuccessful. The Shansi clique were bent on the establishment of a new Government with the co-operation of Wang Ching-wei, and still fancied their military position to be a strong one. From the outset it appeared likely that only a politico-military decision would settle this question, and on the 21st September, as a result of the occupation of Tientsin by the Mukden troops, the former commissioner resumed control of the native customs office. The Mukden policy in regard to the maritime customs-house was then not known, and it was not certain whether the young marshal would definitely declare himself on the side of Nanking. The incident, however, solved itself in a dramatic manner on the 1st October, when Mr. Simpson was shot in the back by three Chinese speaking the Fengtien dialect at the residence of the Commissioner of Customs in the ex-German concession, receiving a wound which completely paralysed him and from which he died some weeks later. Mr. Grierson consequently reoccupied the customs-house on the 3rd October, and resumed control on behalf of the Inspector-General, and all the foreign and Chinese employees engaged by Mr. Simpson were dismissed. While the murder of Mr. Simpson was probably inspired by a political motive, it is impossible to conjecture (and may never be known) whether it was the work of the Nanking, the Mukden or the Shansi faction. It has also been suggested that he was a victim of his dealing with, or endeavours to suppress, opium or drug dealers. The assassins had no difficulty in making their escape, and all representations to the Chinese authorities urging that they should be brought to justice have produced no results. The Chinese police of the First Special Area, where the crime took place, were completely disorganised at the moment of the crime by the political crisis, involving the taking over of Tientsin by the Fengtien army. situation accentuated the normal difficulties inherent in the conflict of police jurisdictions existing within a comparatively small area at Tientsin. Mr. Simpson's short-lived control of the Tientsin Customs was regarded with some favour by local merchants, but whether because, as he himself claimed, he had done much to eradicate the antiquated methods of the customs proper, or because he put the interests of the merchants before those of the revenue, it is hard to estimate. The ease and success with which he carried out his ill-fated coup is unfortunately only too likely to encourage other regional leaders in need of funds to attempt a similar one.

(2) Hong Kong Customs Agreement.

In the earlier part of the year, the prospect of the Hong Kong Government coming to an agreement with the Chinese Maritime Customs over the question of the prevention of smuggling, did not seem very bright. In return for allowing the customs to function in the territory and waters of the colony, the Hong Kong Government were asking that ships under the British flag, registered with the customs for the purpose, should be allowed to trade between the colony and non-treaty ports on the coasts of Kwantung and Kwangsi Provinces, and also that the privileged factory treatment accorded under certain conditions to native factories in China (see the section of this report under "Taxation") should similarly be granted to factories established in the colony. These concessions the Chinese Government were under no circumstances prepared to grant. The question had, therefore, almost reached a deadlock, and the Chinese were openly threatening to take their own measures to put an end to the smuggling, and revive the "blockade" of Hong Kong. On his arrival in Hong Kong in May, the new Governor, Sir William Peel, came to the general conclusion that it would be a mistake to let the Chinese run a preventive service of their own in the waters of the colony, as the encouragement such a footing would give to the "irredentist" tendencies of the Southern Chinese in regard to the colony was a

real danger. He was, however, fully alive to the desirability of assisting the Chinese to put an end to the smuggling, which was undoubtedly being carried on from Hong Kong, and he felt that the best chance of coming to an agreement was on the basis of a scheme of dual control, operated by the Government of the colony and the Chinese customs in collaboration in Hong Kong waters. A draft It such a scheme had already been prepared by Mr. Lioyd, the Superintendent of Customs and Excise. Sir Miles Lampson fully shared the view that it was better to drop the previous draft agreements and concentrate on a solution of the smuggling problem. It was finally agreed that Mr. Lloyd should in the first instance discuss his proposals with Mr. Osborne, the Commissioner of Customs at Kowloon, on the understanding that Mr. Oscorne would be told at the outset that China could never agree to the iniand waters and privileged factory treatment previously demanded. The conversations between Mr. Osborne and Mr. Lloyd aid not promise well at first as Mr. Osborne was instructed to ask as a preliminary condition that the customs should be allowed to open their own stations at various places in the colony, at which all junks must call to have their cargo assessed and examined, and pay all Chinese dues, a situation which would entail Chinese customs launches operating within the waters of the colony, with a view to the detention of junks, and might prove a fruitful source of friction. Later, however, on receipt of a letter from Sir William Peel, saying that his Government were prepared to allow the Chinese customs officers to collect duties on behalf of the customs alongside Hong Kong officials, Mr. Maze set about preparing a scheme, providing for co-operation in the collection of duties and prevention of smugging between Hong Kong officials and seconded customs officers, lent to the Hong Kong Government for the purpose, and to work under the Superintendent of Customs and Excise, but to be paid by the Chinese Government, while customs launches operating in Hong Kong waters were to have Hong Mr. Maze was anxious that full official recognition Kong officials on board. should be accorded to the Commissioner and Deputy-Commissioner of Customs (the former to be British and the latter Chinese) by the Hong Kong Government, and that they should have a definite position in the Government's table of precedence. Mr. Maze's proposals were considered by Sir William Peel to be not unsatisfactory and to offer reasonable hope of an agreement. A fresh draft agreement was accordingly drawn up by the Hong Kong Government on these lines, which Mr. Maze regarded as generally acceptable. The question of precedence of the customs officials was to be settled in a separate exchange of notes. After some amendment of detail, a final draft was agreed upon between the Governor and Mr. Maze, who visited the colony towards the end of October, and was submitted to the Nanking Government and His Majesty's Government for their approval. The Foreign Office decided that, in the event of such approval, the agreement should be signed by H1s Majesty's Minister on behalf of His Majesty's Government and the Chinese Minister for Foreign Affairs on behalf of the National Government, in accordance with the normal procedure, rather than by the Inspector-General of Customs on the one hand and either the Governor of His Majesty's Minister on the other. Unfortunately, as previously stated, and although strongly supported by the Minister of Finance, this draft agreement was turned down by the Central Executive Committee at Nanking in November, on the ground that it would damage the interests of Canton. real basis of the opposition of the Canton elements in the Kuomintang appears to have been the fear that it would run counter to the proposed project for the development of the "free" port of Chungshan (at the mouth of the Canton River delta, some 50 miles from Hong Kong, and 28 miles north of Macao, with which it is connected by road), in which many high Cantonese officials, including Mr. Tong Shao-yi, are personally interested, and through which extensive smuggling was already reported to be going on. The Minister of Finance had apparently made himself unpopular with the Cantonese members of the Executive Committee of the Kuomintang by ordering the institution of a customs corden to circumvent this smuggling. Sir Miles Lampson pointed out to the Minister of Finance that this lightly-taken decision was most regrettable after all the work and effort on both sides, that the Hong Kong Government had gone a long way to meet Chinese wishes in the matter, and he was not personally prepared to press them to make any further concessions. Whatever may be the outcome of any attempt now to establish a preventive service to check smuggling through Hong Kong, the Government of the colony have undoubtedly placed themselves in a

very much better position than they were before to deal with such eventualities by the goodwill they have shown in the negotiations of a reasonable agreement.

358. Apart from the two questions dealt with in detail above, the Inspector-General has been successful in keeping the many important functions of the Customs Administration that are vital to the trade of the country free from the encroachments of other departments of the National Government.

VIII.--AVIATION.

- 359. The past year has witnessed a considerable advance in both civil and military aviation in China, and an increased realisation by the Chinese authorities of the great advantages of this means of communication in a country still singularly deficient in road and rail systems.
- The Shanghai-Hankow air mail and passenger service, which was inaugurated in October 1929 as the result of contracts signed in April of that year, has continued to operate regularly and with a minimum of accidents. Loening Amphibian planes, piloted by foreign (principally American) pilots, are used, and the route followed is that of the Yangtze River. The service is popular amongst the Chinese, and the cost of the return fare from Shanghai to Hankow has during the past year been lowered from 300 to 207 dollars. The time occupied from Shanghai to Hankow, with stops at Nanking and Kiukiang, is seven hours, as against three and a half to four days on the upward and three days on the downward journey by steamer. The friction which developed at the end of 1929 between the operating company, the China Airways Corporation, and the Chinese authorities led to the signature on the 8th July, 1930, of a new Sino-American aviation contract. This contract provides for the organisation of a limited company, known as the China National Aviation Corporation, with a capital of 10 million dollars, divided into 10,000 shares of 1,000 dollars each, 5,500 of which were subscribed by the Ministry of Communications and the balance by the American interests concerned. The contract is to remain in force for ten years, and, in case neither of the contracting parties indicates its desire to cancel it one year before the expiration of this term, it is to remain in force for a further period of five years. It is proposed under the new contract to extend the existing service from Hankow to Chengtu in Szechuan, and to inaugurate two additional services, Nanking to Peiping, and Shanghai to Canton viâ the coastal ports. Trial trips have already been made as far as Ichang, and it is probable that the Yangtze service will be extended to this port before long. Its further extension to Chungking is, however, for the moment held up by the opposition of the Szechuan military authorities, who, it is believed, demand the right to commandeer the planes in the event of an outbreak of hostilities in that province. There are as yet no very definite indications of the inauguration of the other two projected services. A new air mail contract was at the same time (July 1930) concluded between the Directorate-General of Posts and the China National Aviation Corporation, which eliminated the heavy loss to the Post Office in respect of air mail services resulting from the previous contract. Instead of the minimum compensation of 1.50 gold dollars per flying mile payable under the old contract, the corporation receives only the proceeds of whatever mail is carried. This is quite insufficient to meet the running expenses of the service. and everything goes to show that China is hardly ripe for air mail services on any paying basis. The American interests concerned with the contract under the discussion are, however, more interested in popularising their planes than in operating financially successful air lines.
- 361. The contract between the Ministry of Communications and the German Lufthansa Company for the operation of an air mail and passenger service between China and Berlin appears to have been finally signed about the end of 1930. The contract provides for the creation of the Euro-Asia Aviation Corporation, with a capital of 3 million dollars, divided into 3,000 shares of 1,000 dollars each, of which the Chinese Government holds 2,000 and the German company 1,000 shares. There are nine directors, of whom six are Chinese and three German. The corporation is said to have engaged four German pilots, nine mechanics and a supervisor. Junker planes will be used. It is proposed, in the

first instance, to run a service of an experimental nature between Shanghai, Nanking, Tientsin, Mukden and Manchouli, a total distance of 2,500 kilom. Arrangements have to be completed with the Soviet authorities before this service can be extended to Russia and thence to Berlin, a total distance of some 3000 kilom. The ultimate objective is the co-ordination of flying services maintained respectively by the Euro-Asia Aviation Corporation (between Nanking and Manchouli), the Russian "Debrolet" (between Manchouli and Moscow), and the Lufthansa and Deruluft companies (between Moscow and Berlin).

362. The proposed addition to the existing air service, operated by the Japan Air Transport Company, between Tokyo and Dairen viâ Osaka, Fukuoka, Fusan, Keijo and Heijo, of a service between Fukuoka (near Nagasaki) and Shanghai, appears to have fallen through, presumably owing to the opposition of the Chinese Government, in spite of the carrying out of successful test flights in March 1930.

363. An air mail and passenger service on a small scale was inaugurated between Canton and Wuchow in December 1930.

364. While no contracts have been entered into by British manufacturing interests for the operation of air services or the construction and equipment of aerodromes, a considerable number of British planes have been sold in this country during the year under review. Messrs. Arnhold and Co. (agents for the de Havilland Moth machines) and the Far Eastern Aviation Company of Hong Kong (representing Avro-Avian and Armstrong-Siddeley interests) have been particularly active in this direction at Nanking, Mukden, Chungking and Canton, and, as the machines sold have given general satisfaction, it is to be expected that still more considerable sales of British machines will be made during the present year.

IX.—TRADE-MARKS, &c.

365. A new Trade-mark Law was promulgated by the National Government on the 6th May, 1930. This law did not differ in any very material particulars from that issued by the National Government in February 1928, except in so far that the penal clauses, Nos. 39 to 45, of the former law were omitted. This gave rise to anxiety amongst foreign holders of registered marks lest protection under the new law would only be granted in the Chinese courts in cases where actual counterfeiting of a registered mark (punishable under articles 268 and 269 of the Criminal Code) could be proved, and not in cases of colourable imitation only. This anxiety was increased by a judgment given in the Shanghai Special Dictrict Court in June 1930, though this judgment was subsequently repealed on the ground that the new law had not at that time actually come into force. A Government mandate, dated the 25th November, 1930, finally ordered that the law was to come into effect on the 1st January, 1931. Detailed regulations for the enforcement of the Trade-mark Law were published in the "Trade-mark Gazette" of the 15th January, 1931. A written assurance on the question of colourable imitation was finally received by the commercial counsellor to this Legation from the Director of the Trade-marks Bureau in April 1931, to the effect that, according to a ruling of the Legislative Yuan, whilst a distinction is still drawn between counterfeits and colourable imitations, the latter may be regarded as the former in cases where the trade-mark is registered and where there is clear evidence of the intent to deceive.

Copyright.

366. The question of making representations to the Chinese Government with a view to the revision of the Copyright Law of May 1928 (see last year's report), so as to bring that law up to international standards in the protection it affords to the rights of authors, and thereby enable the Chinese Government to adhere in due course to the revised Berne Copyright Convention of 1908, has received the attention of the departments concerned during the past year. An aide-mémoire in this sense was finally handed to the Minister for Foreign Affairs at Nanking on the 25th May, 1931.

X.—LEGISLATION.

367. Under the Organic Law of the National Government of China, which, for the time being, serves in the place of a Constitution, the Legislative Yuan, established at Nanking in December 1928, was empowered to deal with "legislation, budgets, amnesties, declaration of war, negotiation of peaconclusion of treaties, and other important international affairs." Its main work has, in fact, been the codification of laws.

368. The Kuomintang system of government provides that the main principles governing legislation should, when necessary, be laid down in the first place by the Central Political Council, the party organisation responsible for the "direction and control of the National Government in the administration of important affairs." It appears, however, that in practice the Legislative Yuan is allowed plenty of scope, and that, when the Central Political Council does interfere (as it did in the case of the Civil Code), it only indicates in rather general terms certain main principles for the guidance of the Yuan, which then undertakes the drafting of the detailed provisions of laws. The next step is the submission of the draft text to the National Government Council for confirmation and eventual promulgation in the Government "Gazette," whereupon such laws are regarded as duly enacted.

369. Prior to the inauguration of the present system of government at Nanking in 1928, the Chinese Criminal Code and Police Offences Law, as still enforced, were promulgated by the Southern Government, who, however, had little time to undertake further legislation; but, during the past two years, the Legislative Yuan has produced a remarkable mass of legislation dealing mainly with civil and commercial matters. Not only has it revised and caused to be reissued in new form the majority of the main laws of the former Peking régime, but it has also broken a great deal of new ground. Its main task has been the compilation of a complete Civil Code in five books, dealing respectively with General Principles, Obligations, Things, Family Relations and Succession. The first three of these books are already in force, and books four and five come into force on the 5th May, 1931. Connected with the Civil Code come the Civil Disputes Arbitration Law (promulgated the 20th January, 1930), and the Civil Procedure Code, which is not yet quite complete. It is noteworthy that the Chinese Civil Code has been purposely extended to cover certain purely commercial matters, such as commercial contracts, &c., instead of being confined to subjects generally regarded as belonging to a Civil Code; at the same time, the more important commercial subjects have been dealt with separately, and laws relating to Negotiable Instruments (the 30th October, 1929), Insurance (the 30th December, 1929), Companies (the 26th December, 1929), and Maritime Commerce (the 30th December, 1929), have been promulgated independently.

 $370.\,$ Some few of the other main laws promulgated during the past two years, with their dates, are :—

Nationality Law (the 5th February, 1929).
Civil Service Examination Law (the 1st August, 1929).
Army, Navy and Air Force Criminal Code (the 25th September, 1929).
Labour Unions Law (the 21st October, 1929).
Factory Law (the 30th December, 1929).
Army, Navy and Air Force Trials Law (the 24th March, 1930).
Land Law (the 30th June, 1930).
Cinema Censorship Law (the 3rd November, 1930).
Publications Law (the 16th December, 1930).
Opium Suppression Act (the 25th July, 1929).
Chambers of Commerce Law (the 15th August, 1929).
Stock Exchanges Law (the 3rd October, 1929).
Narcotic Drugs Ordinance (the 11th November, 1929).
Law of Petitions of Appeal (the 24th March, 1930).
Trade-mark Law (the 26th May, 1930).
Army, Navy and Air Force Punishments Law (the 7th October, 1930).
Shipping Law (the 4th December, 1930).

371. While due credit has to be given for the work accomplished by the national authorities in so short a period of time, unfortunately the criticism of

the Extra-territoriality Commission in 1926, relative to the practice of promulgating laws whose enforcement is delayed for long periods pending the production of further detailed regulations, still applies; furthermore, the actual enforcement throughout the country of laws nominally in application is still largely subject to the exigencies of political and other considerations. Criticism of the laws themselves has not yet been undertaken. This awaits detailed examination by experts, who alone can decide how far they comply with Western standards of legislation. Unfortunately, such an examination is likely to be retarded by the absence of official and authoritative translations, which the Chinese Government appear to have hitherto deliberately neglected to make.

X1.—Propaganda.

- 372. Apart from the arrangements made by the officially-subsidised and semi-official Kuomin News Agency (which maintains an office in New York) for the transmission of Chinese news to the United States and Europe through the United Press and Transoceanic News services, the National Government is not believed to be undertaking any organised propaganda work in foreign countries with the specific object of furthering its national prestige abroad. The value of propaganda is, however, well recognised, and there is little doubt that there would be more activity in this direction were funds available; as it is every opportunity is taken to propagate the "Nationalist" view-point abroad through the medium of the Chinese representatives in Europe and America and the envoys sent abroad from time to time on official or unofficial missions.
- 373. On the other hand, in China itself and amongst Chinese citizens throughout the world the propaganda work undertaken by the Government is extensive and thorough, and by this means, indirect though it is, foreign opinion is undoubtedly influenced. Thus through the medium of Chinese residents abroad and more recently through the subsidised press in China, as will be shown below, the Government is extending the scope of its publicity abroad.
- 374. This propaganda work may be divided into that undertaken by the Kuomintang and that undertaken by the Ministry for Foreign Affairs through its Intelligence and Publicity Department. It is, however, difficult to determine exactly where the dividing line comes. It must be remembered that under the present system of government the administration of the country is largely controlled by the Kuomintang. It seems likely therefore that the Kuomintang Propaganda or Publicity Bureau similarly controls all activities of a propagandist nature; but authentic information as to this point is not at present available.
- 375. Like the whole party system, the Propaganda Bureau was, in 1924, very efficiently organised at Canton on Soviet lines. It has since then exercised a very considerable influence on national affairs. It was largely responsible for the Hong Kong strike and anti-British boycott of 1925 as well as for the success of the Southern forces in the anti-Northern campaign in the succeeding years. The party branch offices in provincial capitals, municipalities, hsien districts, rural areas and town wards all have their equivalent propaganda organisation. This applies also to military and naval units and to the party branches established amongst Chinese communities overseas. The Central Bureau at Nanking controls the whole system, issues its propaganda pamphlets, slogans, &c., and subsidises, or obtains support from local Administrations for, party newspapers in all the large centres. It also has its own news agency and its own periodicals which have a wide circulation amongst Chinese at home and abroad. It is, for instance, known to subsidise the following Chinese newspapers at Shanghai:—

		Dollars
		a month.
"Eastern Times"	 	1,000
"China Evening Post"	 	500
"Shanghai Evening News"	 	500
"China Times"	 	?
"Shanghai Pao"	 	200
"Shanghai Daily News"		200

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376. Whatever its connexion with the Propaganda Bureau of the Kuomintang, it is understood that the Intelligence and Publicity Department of the Waichiaopu is responsible for subsidising a number of English language news agencies and papers, as well as for undertaking secret service work. The annual sum available to this department is reported to be 360,000 dollars. following agencies, newspapers and periodicals are believed to be subsidised, but it is not possible to vouch for the accuracy of the list or of the figures and it is possible that in certain of the cases the subsidy is provided by the Kuomintang Propaganda Bureau or by some other Government department.

> Kuomin News Agency (official), 5,000 dollars a month. Kuomin News Agency (a separate unofficial agency), 2,000 dollars a month.

Kuowen News Agency

"China Critic" (weekly), 500 to 1,000 dollars a month. "Chinese Nation" (weekly).

"China Weekly Review" (weekly).
"China Press" (daily, Shanghai), newly purchased from British interests

- "Leader" (daily, Peking).
 "Hankow Herald" (daily, Hankow). "Canton Gazette" (daily, Canton). "China Truth" (weekly, Canton).
- Under its organisation the Intelligence and Publicity Department is responsible for the following matters:-
 - (1) The collection of intelligence reports on internal and external affairs.

(2) Publicity regarding the foreign policy of the Government.(3) The translation of Chinese and foreign press notices.

(4) The interviewing of the press.

(5) Other matters related to No. (1) above.

The department has five sections and including the director (at present Dr. M. T. Z. Tyau, L.L.D.) has a staff of thirty-nine persons, with pay roll of 6,350 dollars a month, out of a total establishment of 336 persons employed in the Waichiaopu.

- There have, during the past two years, been occasional references to a proposal to form an International Publicity Bureau, but no steps seem to have been taken as yet to put this scheme into effect.
- 379. In Mukden, the Vice-Commander-in-chief, Chang Hsueh-liang, has a propaganda organisation called the "Committee for Public Enlightenment." This committee apparently does little more than issue occasional bulletins concerning Manchurian affairs. The members of the committee receive no pay for their services, but their actual expenses are defrayed by Chang Hsueh-liang.
- The commercial and cultural propaganda activities of the Government are of little importance. The Ministry of Industry maintains a "Bureau of Industrial and Commercial Information" at Shanghai, which publishes a useful weekly bulletin, the "Chinese Economic Bulletin," and an equally useful monthly journal the "Chinese Economic Journal." There is also an institution at Nanking known as the Academia Sinica, which aims at being the centre for educational and cultural activities in China. So far it seems to be confining itself to purely national undertakings.

XII.—CLAIMS.

381. The assessment of seven individual claims for losses incurred at Pukow and Puchen at the time of the Nanking incident in 1927 was commenced in December 1929 by a somewhat informal mixed commission (see paragraph 434 of the report for 1929), and was completed in January: the amount finally awarded was 61,800 63 dollars, representing an average deduction of about 21 per cent.

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No payments have yet been made by the Chinese authorities in respect of these claims.

382. After repeated efforts on the part of His Majesty's Minister to press the Chinese Government to pay further instalments in settlement of the balance outstanding on account of the Nanking claims (which, it will be recalled, had been finally assessed during the previous year by a mixed Sino-British Claims Commission), the Chinese Government undertook in May to pay instalments of 100,000 dollars up to August, when these would be increased to 200,000 dollars until the balance had been liquidated. This promise was, however, not carried out; one instalment of 100,000 dollars was received and distributed pro rata to individual claimants, but no subsequent instalments were received up to the end of the year, though since then further payments have been made, and are now being distributed.

383. The Communist occupation of Changsha at the end of July resulted in considerable looting and destruction of property, and two British firms—Messrs. Jardine, Matheson and Co., and the British-American Tobacco Company (Limited) suffered losses amounting in each case to over 100,000 dollars. The statements of claim will be formally presented to the Chinese authorities in due course, but it is understood that the American Legation has been informed that the Government repudiates all liability in these cases.

384. In February His Majesty's Legation received a despatch notifying the definite adoption by His Majesty's Government in the United Kingdom of the policy of not presenting (except in certain special circumstances) claims for losses of goods in the hands of native agents. This decision is one result of the general tendency now manifesting itself to scrutinise more closely the grounds for liability of the Chinese Government in the case of claims for compensation. His Majesty's Minister has moreover suggested that a special preparatory claims commission be set up to overhaul the lists of existing British political claims, with a view to their reclassification in readiness for the time when a settlement may come under consideration.

XIII.—Who's Who.

(An index to the Who's Who of the last five years is included. The figures after names refer to previous Annual Reports.)

Chan Chai-t'ong. (See Ch'en Chi-t'ang.)

Chan Ming-shu. (See Ch'en Ming-shu.)

Chang Chen (Chang Kang-chih). 1928. In 1929 commanded 1st Division of the Government troops at Amoy, concurrently Commander-in-chief of Bandit Suppression. March 1929 elected reserve member, Kuomintang Central Executive Committee. In 1930, faced with serious bandit and Communist situation in Fukien, he preferred inactivity to possible defeat, but nevertheless throughout the year preserved comparative order in the districts under his immediate command. In November 1930 promoted member of Kuomintang Central Executive Committee, and in December appointed to command 49th Division and instructed to undertake active anti-Communist campaign.

Chang Chih-chiang. 1926. In 1928 member of Government Council, Nanking; October 1928–November 1930 chairman of National Opium Suppression Commission; November 1930 appointed Bandit Suppression Commissioner for Kiangsu.

Chang Ch'un. Born 1888, native of Szechuan. Graduate of Paoting Military Academy and Tokyo Military Staff College. 1920 Chief of Police, Chengtu; 1922 Chief of Police, Kaifeng (Honan); 1927 attached to Northern expedition; 1928 Director of Shanghai Arsenal, political Vice-Minister of Military Affairs. Member of Kuomintang Central Executive Committee and Mayor of Shanghai since March 1929. Early in 1930 he was sent to Foochow to settle the crisis following the coup d'État there, but returned on the assassination of his secretary. Absent from Shanghai for prolonged periods throughout 1930 at Tsinan and Mukden, acting as go-between for the Central Government.

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Chang Fa-k'uei. 1927–28–29. Early in 1930 he led his famous "Ironsides" south from Hunan into South Kwangtung, where they terrorised the country side. Associated with Ch'en Chi-t'ang and Li Tsung-jen in their attacks on Kwangtung, but the operations did not prosper, and when fighting broke out in the North, Chang invaded Hunan with Pai Ch'ung-hsi and Li Tsung-jen, capturing Changsha in June. Attacks from Kwangtung forced them back, however, and Chang spent the remainder of the year in desultory operations against the Canton forces. His relations with Ch'en Chi-t'ang were strained on more than one occasion.

Chang Fu-yun. 1928.

Chang Hsiao-liang (this is the spelling officially adopted for the transcription of his name into English, but Chang Hsueh-liang is still commonly used). 1926-27-28-29. Chang remained strictly neutral during the first half of 1930, resisting the blandishments of both the Central Government and the northern coalition, and in fact denying himself to visitors as much as possible. His difficulties were increased by Communist activities at Mukden, but, beyond reinforcing the Manchurian troops in North Hopei, he took no active measures to indicate the nature of his plans-which were indeed indefinite, dependent to a great extent on the outcome of events elsewhere in China. After suppressing a threatened revolt among his troops inside the wall, he inaugurated the new harbour works at Hulutao on the 3rd July, and then, assisted by a convenient wash-out of the railway, he succeeded in retiring to Peitaiho and so evading the awkward deputations of wooers from both factions. He returned to Mukden on the 30th August, and on the 18th September, at the conclusion of a conference with the heads of the four provinces of Manchuria, decided to issue his famous "Peace Manifesto," at the same time despatching troops to occupy Tientsin. This virtually ended the civil war. Went to Nanking personally in November, thus finally demonstrating his sympathies with the Central Government. His physical condition showed steady progress throughout the year, although at one time in the summer it was feared that there were signs of a recrudescence of his drug-taking habits. In view of his difficult and delicate position vis-à-vis the civil war factions, the Sino-Russian negotiations in Moscow, and the reactionary elements in Manchuria itself, it must be conceded that he played his hand throughout the year with considerable skill.

Chang Hsiao-ming (Chang Hsueh-ming). Brother of Chang Hsueh-liang—his chief title to distinction. Fond of comfort and good living, he did not come into prominence until he was appointed Chief of Police at Tientsın when the Manchurian troops took possession of the city in November 1930.

Chang Tso-hsiang. 1927–28. Governor of Kirin Province and Deputy Commander-in-chief of North-Eastern Defence since December 1928. Appointed State Councillor of the National Government, December 1930. One of the Manchurian "Higher Council," he was instrumental in keeping Manchuria out of the civil war until intervention could further Manchurian interests.

Chang Tsung-ch'ang. 1925-26-27-28-29. "Champion bad Chinaman," he remained in Japan throughout 1930 with his numerous wives and accumulated funds. It was, however, rumoured that he might yet attempt a come-back, if he could find a party ready to accept him.

Chao Heng-t'i. 1926.

Chao Tai-wen. Born at Wut'ai in Shansi, 1867. Defence Commissioner, Northern Shansi, 1916; 1928 chairman of Chahar Provincial Government; 1929–30 Minister of the Interior and vice-chairman of the National Commission for Mongolian and Tibetan Affairs; member of Kuomintang Central Executive Committee; State Councillor and president, Control Yuan. Chao, Yen Hsi-shan's cleverest and most trusted civil adviser, resigned his post as Minister of the Interior in February 1930, and proceeded to Shansi in March, where he remained, taking an active part in directing the anti-Chiang movement. In November 1930 he was expelled from the Kuomintang and dismissed from all his posts.

Ch'en Chiung-ming. 1925-26.

Ch'en Chi-t'ang (Chan Chai-t'ong). 1929. Has commanded the VIIIth Route Army since 1929. Busy early in the spring of 1930 directing operations against the Kuangsi "rebels"; but, when hostilities broke out in the North, both sides marked time for a while. Ch'en repeatedly avowed his loyalty to Nanking, which had sometimes been doubted; it was rumoured that his loyalty was purchased by Nanking for a large sum, and he justified the investment by pursuing the Kuangsi forces into Hunan in June and forcing them to abandon their plan to march on the Yangtze. He is said to have had a secret understanding with the Kuangsi leaders, and also with Wang Ching-wei; in any case, he continued nominally to conduct singularly indecisive operations against the Kuangsi forces for the remainder of the year.

Ch'en Chung-ming. Native of Kwangtung, born 1875; 1917 Minister of War in the Canton Government; 1921 Civil Governor of Canton and Commander-in-chief of the Kwangtung forces. Proscribed by the National Government for betraying Sun Yat-sen in 1922.

Ch'en Ming-shu (Chan Ming-shu). 1928–29. Chairman of the Kwangtung Provincial Government since 1928. March 1929 re-elected member of the Kuomintang Central Executive Committee. With the aid of his doubtful ally, Ch'en Chi-t'ang, he was successful in repelling the attacks of the Kuangsi forces on his province, and, when the latter invaded Hunan in May, Chen took possession of Kuangsi. In October he visited Nanking to discuss the situation in the south and to consolidate his own position vis-à-ris Ch'en Chi-t'ang. Successful in stopping the negotiations between the Minister of Finance and the Hong Kong Government for the conclusion of a customs agreement.

Ch'en T'iao-yuan. 1926–27–28–29. Astute politician, he definitely threw in his lot with Nanking early in 1930, during the crisis in Shantung, an action which surprised and embarrassed the Feng–Yen coalition. On the recapture of Tsinan in August and the appointment of Han Fu-ch'u as chairman of the Provincial Government, Ch'en was appointed to his old post of chairman of the Anhui Provincial Government.

Ch'en Tu-hsiu. 1927. Expelled from the Kuomintang in 1928 for his Communist affiliations.

Ch'en Yu-jen (Eugene Chen). 1925–26–27. Elected a member of the Kuomintang Central Executive Committee and Central Political Council, 1929–30; but at the end of 1930 was still in Europe.

Cheng Ch'ien. 1927-28.

Cheng Shih-ch'i. 1925-26.

Ch'i Hsieh-yuan. 1925-26

Chiang Chung-cheng (Chiang Kai-shek). 1925–26–27–28–29. Ambitious, dictatorial, and narrow, Chiang's power of subtlety and intrigue, his military experience and ability, and his strong will, brought him in 1930 successfully through the worst storm he had encountered since the termination of the anti-North campaign in 1928. Very much a "lone eagle," he irritated his colleagues and subordinates by failing to keep them informed of the course of events; he confided in only two or three of his most trusted friends, and made his own plans—even to the extent of disregarding the advice of his German military advisers on occasion. He spent little time at Nanking, and by incessant activity he sought to visit all the fields of battle and direct operations personally. Whilst his continuance in power at the end of the year was undoubtedly due in large measure to his own remarkable qualities, the strain was beginning to tell, and, physically tired and financially exhausted, he did not seem at the end of 1930 to realise his growing unpopularity in party circles, though (at the request of Chang Hsueh-liang), he issued some manifestos promising a wider basis of government. It appeared, however, that he had no intention of implementing these promises, and seemed to consider that he could afford to ignore the discontent in the party if he consolidated his military position by an alliance with Manchuria.

 $Chin\ Yun\mbox{-}ao.$ 1926–27. Member of National Military Council since June 1930.

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Chin Yun-p'eng. 1927. Living in retirement in Tientsin.

Chou Feng-ch'i. 1927.

Chou Hsi-ch'eng. 1929.

Chou Yin-jen. 1925-26.

Chu Chao-hsin. 1927-28. August 1927-May 1929 Vice-Minister for Foreign Affairs, Nanking, and concurrently Commissioner for Foreign Affairs at Canton.

Chu P'ei-te. 1927–28. Member of Kuomintang Central Executive Committee since 1926, and member of Kuomintang Central Political Committee since 1928; member of National Government and Chief of the General Staff since 1929.

Chu Yen (Tchou Yen). Belgian returned student, member of French Municipal Council, French Concession, Shanghai; pro-French sympathies. In charge, during 1930, of the Land Bureau of the Municipality of Greater Shanghai. Said to be a well-meaning and reasonable man, but thin-skinned and apt to take offence.

Ch'u Yu-p'u. 1927-29.

Fan Shih-sheng. 1925-26-27

Fana Chen-wu. 1926-29.

Fang Pen-jen. 1925–26. In 1928 a member of the Taiyuan branch of the Kuomintang Central Political Council; 1929–30 a member of the Hupeh Provincial Government; January 1930 came to Peking as a representative of Chiang Kai-shek.

Feng Yu-hsiang. 1925–26–27–28–29. In the early part of 1930 was living near Wut'ai, in Shansi, as the guest (or prisoner) of Yen Hsi-shan, urging on his more cautious host the desirability of an immediate attack on Chiang Kai-shek. When the war finally started, his troops bore the brunt of the fighting, Feng's personal qualities as a leader compensating the enemy's superior equipment. On the collapse of the rebellion in the autumn Feng retired to Shansi, where he wandered about the countryside attended only by two or three bodyguards.

Fu Ping-ch'ang (Foo Ping-sheung). 1925–26. In 1927 Director of the Customs Administration and chairman of the Tariff Commission, Nanking. Member of Legislative Yuan and chairman of its Foreign Relations Committee since December 1928; March 1929 appointed Minister to Belgium, but did not proceed.

Fu Tso-yi. Born 1895; graduate of Paoting Military College. 1926 promoted division commander for defence of Tientsin. 1927 successfully defended Chochou (Peking-Hankow line) for Nationalists against Mukden forces. 1928–30 garrison commander of Tientsin. In March 1930 he led a force of 9.000 men into Shantung as the first move in the anti-Nanking campaign. A good soldier, and might, by the subjugation of Shantung in July and August, have turned the scale against Nanking had it not been for the jealousies amongst the Northern commanders, which kept him from the pursuit of Han Fu-ch'u.

Han Fu-ch'u. 1929. Held a key position in Shantung at the beginning of 1930, and to ensure his loyalty Chiang Kai-shek was obliged to pay large sums, which induced him to declare definitely for Nanking to the great embarrassment of the Northern generals, who had hoped to secure his services for themselves. In mid-April he was entrusted with the defence of the country south of the Yellow River, but in June was forced to abandon Tsinan. During July constant attempts were made to lure him away from allegiance to Nanking, but the negotiations failed not on account of his loyalty to the Central Government but because the Northerners would not accept his terms. When the Shansi troops were finally routed Han was sworn in as chairman of the Shantung Provincial Government (the 10th September), and spent the remainder of the year in a fairly determined drive against bandits. A doubtful but useful ally to any side; a good disciplinarian and successful in keeping his men in order and well-drilled.

Han Kuo-chun. 1925-26.

Han Yu-k'un. 1926.

Ho Chien. 1926-27-28-29. Chairman of the Hunan Provincial Government since April 1929. His loyalty to Nanking has often been in question; at any rate, he is a practised and successful fence rider, and showed no eagerness to become seriously involved on either side when the Kuangsi forces invaded Hunan in May and June 1930. Ho withdrew temporarily from Changsha to allow the invaders to occupy the city, a manœuvre which he repeated the following month, when the Communists captured the city at the end of July. Ho was still in power at the end of the year.

Ho Ying-ch'in. 1927–28–29. March 1930 appointed Minister of Military Affairs. In high favour with the Central Government.

Hsia Ch'ao. 1926.

Hsiao Yao-nan. 1925-26.

Hsieh Ch'ih. Went to Shansi from Tientsin in March 1930, on the instructions of Wang Ching-wei, to negotiate with Yen Hsi-shan on the organisation of the coalition and establishment of a Government. Returned to Peking in May to await Wang's arrival. One of the seven members of the Peking Government when it was inaugurated in September. Fled to Shihchiachuang later in the same month, to Tai Yuan in October, and finally to Tientsin. One of the leaders of the Western Hills party.

Hsiung Shih-hui. Native of Kiangsi, graduate of Tokyo Military Staff College. 1926 commander, 1st Division; member of the Kiangsi Provincial Government; commander, 37th Division, XIIIth Army. Since September 1928 commander, 5th Division, and concurrently garrison commandant for Sungkiang and Shanghai. In May 1930 was appointed concurrently Bandit Suppression Commissioner for Kiangsu, Anhui and Chekiang. On the 9th December he was seriously injured in an aeroplane accident.

Hsu Ch'ien (George Chien Hsu). 1927. Regarded as a Communist and proscribed by National Government since 1927.

Hsu Shih-ying. 1925-26. Chairman of the National Famine Relief Commission since December 1928.

Hse Tsu-shan, D.S.O. Native of Kiangsu, born 1890. Graduate of Nanking Naval School; graduate of Massachusetts Institute of Technology; during war attached to Chinese naval mission in England. Appointed High Commissioner for Weihaiwei on its rendition, October 1930, and proved himself a successful and capable administrator. A personal friend of C. T. Wang, T. V. Soong, &c., and an ardent Nationalist, but lukewarm in his adherence to the Tangpu system.

Hu Ching-yi. 1925-26.

Hu Han-min. 1925–26–27–28. A strong supporter of the party, and a leader of the "pure party" group; found growing friction in his relations with Chiang Kai-shek and the governing clique in Nanking.

 $Hu\ Jo\text{-}yu$. 1927–28. Again attacked Yunnan in 1929, but was driven out by Lung Yun early in 1930 and fled to Chengtu.

Hu Jo-yu (J. F. Hou)—no relation of the other Hu Jo-yu. Native of Anhui; lawyer; former director of the Peking Octroi; political Vice-Minister of Health and of the Interior; protégé of Chang Hsueh-liang; appointed Mayor of Tsingtao on the 4th September, 1930, but was continually absent from his post serving as go-between for Nanking and Mukden during latter part of the year.

Hu Shih. 1925–26. Attached to Kwang Hua University, Shanghai, and president of Chinese National Institute since July 1927. Noted for his outspoken utterances and frank criticisms of China and things Chinese. Probably the only civilian in China whom the Government would not dare to touch.

Hu Tsu-t'ung (T. F. Woo). Native of Ningpo, educated at Birmingham. General manager of the Bank of Communications, Shanghai, and chairman of the Shanghai Bankers' Association; elected to Shanghai Muncipal Council the 5th September, 1930.

Ho Tsung-to. 1928.

Huang Ch'i-hsiang. 1927.

Huang Fu. 1927–28. Vice-chairman of the Huai River Conservancy Commission since 1929.

Huang, Gaston (Wong Keung). Governor of Hainan early 1930; fled to Canton.

Huang Shao-hsiung (Wong Shiu-hung). 1927.

I P'ei-chi (Yi P'ei-chi). 1928. April 1928–November 1930 Minister of Agriculture and Mining; December 1930 appointed President of Peking Normal University.

Kao Wei-yuen. 1927.

Ko Ching-en. Native of Chekiang, graduated from a Japanese officers' military training school, and was for many years on faculty of Whampao Military Academy; later on General Staff at Nanking. Appointed Mayor of Tsingtao, March 1930.

Ku Wei-chun (V. K. Wellington Koo). 1926–27. For long out of favour with the Central Government, he returned to China in 1930, and became prominent as an adviser to the Mukden Government. The proscription against him was removed by the Nanking authorities towards the end of the year.

K'ung Hsiang-hsi (H. H. Kung). 1928. Minister of Industry since May 1928; reserve member of Kuomintang Central Executive Committee and Central Political Council since early 1929.

K'uo Sung-ling. 1925-26.

Kuo Tsung-hung. 1926.

Lai Hsin-hui. 1926-29

Li Chi-shen (Li Chai-sum). 1927-28-29.

Li Chin-lun (Frank W. Lee). Native of Kwangtung, born 1884. American returned student. 1917 secretary to Sun Yat-sen; 1918–20 director, Political Affairs Department, Ministry for Foreign Affairs, Canton Military Government; 1920–22 Commissioner for Foreign Affairs and Customs Superintendent, Canton; 1922–27 attached to Shanghai College; 1927 director, Political Affairs Department, Ministry for Foreign Affairs; representative of Nationalist Government in United States; member of the Permanent Court of Arbitration, The Hague; October 1928–November 1929 Minister to Mexico; Political Vice-Minister for Foreign Affairs since December 1929.

Li Fu-lin (Li Fuk-lam). 1927.

Li Ming-chung. 1926.

Li Tsung-jen. 1927–28–29. Early in 1930 was engaged in sporadic attacks on Kwangtung; in March captured Pakhoi and Limchow. In April reported to have assumed office under Yen Hsi-shan, and for the remainder of the year took part (on the Kuangsi side) in the desultory fighting between the Kuangsi and the Canton forces.

Li Yueh-kai. Born near Tengyueh, 1882. In 1930 appointed first director of the First (Tengyueh) Frontier Colonisation Bureau. Classical scholar; held various posts in the Shan States and Yunnan before the present appointment.

Liang Shih-yin. 1927.

Liao Chung-kai. 1925-26.

Lin Kuo-keng, C.M.G. 1925-26.

Liu Chen-hua. 1929. Appointed (November 1930) Bandit Suppression Commissioner for the borders of Honan, Shansi and Shensi.

Liu Chen-nien. 1929. His sympathies in the North-South quarrel were all with the North, but whilst declining to obey the orders of Nanking, he took no active steps to assist either side, and, supplied with arms from Japanese sources, he remained in control of Chefoo aloof from the civil war. In March he declared open war on Nanking, but still refrained from taking a very active part, and gradually drifted back to the position of nominal supporter of Nanking, whose

authority over him was very slight. Still in power at the end of 1930, thanks, it is said, to an arrangement with Chang Hsueh-liang. A strong and efficient administrator.

Liu Chi-wen. Born 1890, native of Kwangtung; graduate of Tokyo Law College. 1926 Commissioner of Agriculture and Labour, Canton; Quarter-aster-General, Commander-in-chief's headquarters; April 1928-March 1930 Mayor of Nanking, where he proved himself keen on his work but somewhat lacking in authority over his staff. In April 1930 he was appointed Superintendent of Customs, Shanghai. Member of Kuomintang Central Executive Committee since March 1929.

Liu Hsiang. 1925–26–27–28–29. Continued throughout 1930 with his uncle, Liu Wen-hui, to control Szechuan, despite feeble attempts of the "allied generals" to oust them from their position, which was strengthened by Liu Hsiang's friendship with the Central authorities. In severe financial straits at the beginning of the year, from which he extricated himself by juggling with the opium and salt taxes. Nanking kept him in good humour by supplying him with arms and silver, and towards the end of the year it became clear that Liu Hsiang was definitely to be the instrument for carrying out in Szechuan the policy of the Central Government. A satisfactory and fair ruler from the point of view of foreign interests.

Liu Wen-hui. 1926–29. Throughout 1930 he maintained (though at the end of the year only with some difficulty) a position of unstable equilibrium, with one foot in either camp—allying himself with his nephew whilst at the same time negotiating with the "Northern" generals, T'ien Sung-yao and Teng Hsi-hou.

Lu Chung-lin. 1926. Right-hand man and Chief of Staff of Feng Yu-hsiang. Reported to be a good strategist and certainly a good leader. When hostilities commenced early in 1930 he established his headquarters at Chengchow, which led to an extensive bombing of the city.

Lu Hsiang-t'ing. 1926.

Lu Hsing-pang. Military leader in Fukien. Ex-brigand, illiterate and superstitious, he was employed at one time by Sun Yat-sen. Owing to the success of his operations as a bandit, he was taken into the Provincial Government service. In January 1930, with his brother, Lu Hsing-yun, engineered the arrest of six members of the Provincial Government, who were conveyed to his head-quarters and detained there for several months. He sent telegrams to the Central Government affirming his loyalty, and stating that the prisoners were being detained only until the results of the Central Government investigations were made known-protestations which were somewhat discounted when he refused to obey the orders of Nanking to release them. Early in 1930 he stopped the Communist advance in North-West Fukien, of which he was the virtual ruler. Revolted against the Provincial Government in the summer, and was suspected of affiliations with the Northern rebel Government; but he was unsuccessful in his attempts to capture Foochow, and in September was driven up the river. About this time he figured prominently in the incident of the capture of two English women missionaries, who were being held in territory controlled by him, and who could probably have been saved but for his callous indifference to their He returned, however, to official favour, and was appointed Bandit Suppression Commissioner in West Fukien in October, and by the end of the year was once more one of the leading lights of the Provincial Government.

Lu Yung-t'ing. 1926.

 $Lu\ T'i-p'ing$. 1929. Chairman of the Kiangsi Provincial Government since 1929.

Lu Yung-hsiang. 1925-26.

Lung Yun. 1925–26–27–28–29. Commenced the year by bringing to a successful conclusion his operations against the three "enemy generals," Chang Ju-chi, Hu Jo-yu and Meng-Yu-jen, and driving them into South-West Szechuan. He then devoted himself to increasing the profits of the opium trade and to organising a futile punitive force to invade Kuangsi. This force returned to Yunnan towards the end of the year, having lost thousands of men.

Ma Fu-hsiang. 1925–26. Native of Kansu, born 1876. Graduated in Imperial examinations; brigadier-general for suppression of Boxer outbreaks; 1912, chief administrative officer in Kokonor; 1913–15, Defence Commissioner of Altai and Ninghsia; 1920, Civil and Military Governor of Suiyuan; 1924, Director-General, Aeronautical Department; 1927, member Military Council; 1928–29, member Honan Branch, Kuomintang Central Political Council; vicchairman, National Commission for Mongolian and Tibetan Affairs. Early in 1930 appointed Mayor of Tsingtao; Commander-in-chief, IXth Route Army; April-October 1930, chairman of Anhui Provincial Government; in November appointed chairman of National Commission for Mongolian and Tibetan Affairs. One of the few prominent men at Nanking who seemed genuinely anxious to draw the various parties together.

Ma Hsu-lun. 1926. Political Vice-Minister of Education during 1928 and

Ma Tsu-yuan. 1926.

Mo Teh-hui. Native of Fengtien. 1924, Vice-Minister, Agriculture and Commerce; 1926, Civil Governor of Mukden; 1927–28, Minister of Agriculture and Commerce; president of Chinese Eastern Railway; appointed Chinese envoy to Moscow to negotiate a settlement of the Sino-Russian dispute. After prolonged discussions at Nanking, he finally left Mukden for Moscow on the 1st May, 1930. Protracted negotiations followed, shelved when Mo returned to Berlin on the 29th December on leave of absence.

Pai Ch'ung-hsi. 1927–28–29. March 1930 expelled from the Kuomintang. Engaged in sporadic attacks on Kwangtung throughout the year.

Pao Yu-lin. In 1928 chief of police at Peking; later chief of police at Harbin; in October 1930 once more appointed to Peking. A sensible, pleasant official, who has more than once been helpful in matters affecting British interests.

P'an Fu 1927

Shang Chen. 1927. In 1928 commander of Shansi troops in Peking and Tientsin; 1929, chairman of Hopei Provincial Government; found himself in an anomalous position as chairman of the Shansi Provincial Government early in 1930, suspected by Yen and given very little real power. However, he followed Yen's fortunes more or less faithfully and was appointed acting garrison commandant, Peking and Tientsin areas; appointed as the nominee of the Central Government to be chairman of the Shansi Provincial Government after the defeat and flight of Yen Hsi-shan. Not a Shansi man (his native place is Pao Ting, Hopei), he is distrusted by the other Shansi generals, who will probably lose no opportunity to get rid of him. Reserve member of the Kuomintang Central Executive Committee since March 1929.

Shen Jui-lin. 1925–26. Adviser to North-Eastern Frontier Defence Headquarters since 1929.

 $Shih\ Chao-chi$ (Alfred Sze). 1926. In February 1929 reappointed Minister to Great Britain.

Shih Yu-san. 1929. Started the year by looting Pengpu, which nearly caused a major political crisis. This notorious "grey" general, whose allegiance to Nanking was a purely financial question, was bought off by the Central Government early in the year, but in the spring reverted to the Northern side, assisting Fu Tso-yi in the campaign against Shantung in May and June. He established his headquarters at Tsaochow and adopted a policy of inactivity, awaiting the outcome of actions elsewhere. He continued, however, to be regarded by both sides with great suspicion, and his men (unreliable part-time bandits) were extremely unpopular wherever they went. It was reported at the end of the year that he had come to an arrangement with Chang Hsueh-liang.

Sun Ch'uan-fang. 1925–26–27–28. Lived in retirement at Dairen in 1929; emerged early in 1930 to take part in Mukden politics. It was probably only lack of opportunity and incentive which prevented Sun from taking a more active part in events in 1930 and once more assuming his old rôle of Fengtien free-lance.

Sun K'e (Sun Fo). 1927–28. Member of the Kuomintang Central Executive Committee and Central Political Council since 1926. Vice-president of the Examination Yuan and Minister of Railways since October 1928. January 1929–April 1930, president of the National Aviation Corporation.

Sun Liang-ch'eng. 1929. One of the Kuominchun generals who made terms with Nanking and was sent south of the Yangtze on bandit suppression work.

Sun Yueh. 1925-26.

Sun Ch'ing-ling (Mrs. Sun Yat-sen). 1927. Returned to China in 1929 to attend her husband's State burial. She has since resided at Shanghai, where her house is a favourite meeting-place of politicians.

Sung Tze-wen (T. V. Soong). 1927–28. Vice-president of the Executive Yuan since January 1930 and Minister of Finance since May 1928, in which capacity the insurmountable difficulties which he has encountered have more than once led to rumours of his resignation. The desperate financial straits in which the Government found themselves during the summer caused Soong to have recourse to various illicit methods of raising money to meet the insatiable demands of the militarists unpopular with the North.

Tai Ch'uan-hsien (Tai Chi-t'ao). 1928. President of the Examination Yuan since October 1928.

T'an Yen-k'ai. 1925–26–27–28. Died in September 1930. Had occupied before his death the second place in the hierarchy of the National Government, but was more of a figure-head than a real force in the counsels of the Government. Much respected as one of the Fathers of the Revolution.

T'ang Chi-yao. 1925-26-27.

T'ang San. 1928.

T'ang Shao-yi. Born Kwangtung 1860; one of first Chinese students to go abroad; 1896 consul-general in Korea; 1907 Governor of Fengtien; 1908 Special Envoy to United States; 1912 first Premier of the Republic; 1918 member of Canton Military Government; adviser to National Government since 1929.

T'ang Shen-chih. 1926–27–29. After the failure of his movement against Chiang at the end of 1929 he was proscribed by the Central Government, and early in 1930 Yen Hsi-shan succeeded in eliminating him from the political arena by inducing him to go abroad with money provided by the Nanking Government.

T'ang Sheng-ming. Younger brother of T'ang Sheng-chih. Came into some prominence in 1930 as a leader of the rebel forces (in Hunan) in the attacks on Changsha.

T'ang Yüeh-liang. 1929.

Tchou Yen. (See Chii Yen.)

Teng Hsi-hou. 1926. Commander-in-chief VIIth Route Army, 1928; concurrently member Szechuan Provincial Government and Commissioner of Finance since January 1929. One of the Northern generals in more or less open rivalry with Liu Hsiang. Engineered the arrest of Lo Tse-chow at the end of the year.

Teng Ju-cho. 1925-26.

Ting Wen-chiang (V. K. Ting). 1925-26.

Ts'ai T'ing-kan. 1925–26. Retired in May 1927 and is now living at Dairen.

Ts'ai Yuan-p'ei. 1928. President Academia Sinica since October 1928, and member of Kuomintang Central Political Council since 1926.

Ts'ao K'un. 1925-26.

Tseng Tsung-chien. 1926. Minister to Sweden and Norway, 1926–28; Chinese manager of Peking Syndicate; January 1929, appointed Secretary-General to the Commission for the Readjustment of Finance.

Tsung Chien. 1925.

Tu Hsi-kuei. 1926.

Tuan Ch'i-jui. 1925-26. Retired and lives in Tientsin.

Tung Ho-ch'ing. 1926.

Wang Cheng-t'ing (C. T. Wang). 1926–28–29. Established his reputation in the eyes of the public during 1930 by bringing many negotiations with various foreign Powers to a successful conclusion; but it is doubtful whether he is held in equally high esteem by the Government. He is said to have lost much prestige with the President by his unfortunate handling of the Sino-Russian dispute, and there is a general impression that he is disliked and distrusted by the members of the Central Government, who use him merely because he is an able and unscrupulous agent for handling foreign affairs. Was still Minister for Foreign Affairs at the close of 1930. Said to have organised the trade in official posts under his control in a highly business-like manner.

Wang Ching-ch'un (C. C. Wang). 1925-26.

Wang Ching-wei (Wang Chao-min). 1925–26–27–28–29. Lived in hiding in Hong Kong during the early part of 1930; on the 1st March issued a circular telegram denouncing Chiang Kai-shek, and when his negotiations with the Northern military leaders had reached a sufficiently advanced point, he finally emerged from seclusion and travelled to Peking, arriving there on the 24th July. He devoted himself to the task of organising a Government nominally under Yen Hsi-shan, whom he met at Shihchiachuang in August. The task of organisation was completed in September, but with the intervention of Chang Hsueh-liang and the retirement of the Northern forces, Wang fled to Shansi, and thence, in November, made good his escape from China viâ Tientsin.

Wang Ch'ung-hui. 1925–26–27–28–29. Continued to hold his various Government posts throughout 1930; in September was elected a member of the International Court at The Hague. Kept somewhat aloof from politics during the year, immersing himself in his task of drafting new codes and laws, the annual output of which has now reached torrential proportions.

Wang Po-ch'un. 1928. Member of the Kuomintang Central Executive Committee since June 1929; member of the Kuomintang Central Political Council since November 1930.

Wang Chu-ch'ang. Native of Liaoning. Graduate of Tokyo Military Cadets School; 1921, Chief of Staff Heilungkiang; 1925, Chief Counsellor to Chang Tso-lin; 1926–27, commander 10th Division Fengtien IIIrd and IVth Army Corps; 1928, director of the Bureau of Border Defence; 1930, member of the Heilungkiang Provincial Government; December 1930, took office as chairman of Hopei Provincial Government.

Wei I-san. 1926.

 $Wu\ Ch'ao$ -ch'u. (C. C. Wu). 1925–27–28. Minister to United States since February 1929.

Wu Chun-sheng. 1927.

Wu P'ei-fu. 1925–26–27–28. During 1929 and 1930 was living in retirement in Szechuan, near Suiting, headquarters of Liu Ts'un-hou, Lord of the Szechuan-Shensi Marches. Every party was at one time said to have a representative with Wu, and there is no doubt that his popularity amongst the people is still considerable. There were constant rumours that he was about to come out from his retreat in favour of one party or another, and in June 1930 he did indeed make an unsuccessful attempt to go to Hankow "to act as mediator in regard to the general situation." His way barred, he returned to his headquarters.

Wu T'ien-ch'eng. 1926. Member of the Kuomintang Central Executive Committee since 1928. Member of the Legislative Yuan; April 1930, appointed Political Vice-Minister of the Interior. Acted at various times throughout 1930 as go-between for Nanking and Mukden.

Yang Sen. 1925–26–27–28–29 The stormy petrel of Szechuan; he attended a conference of the "allied" generals (the anti-Liu combine) at Chengtu on the 10th February, 1930, the headquarters of his badly-paid XXth Army being at Chuhsien; subsequently appointed by the National Government Warden of the Szechuan–Shensi Marches. An alliance with Liu Hsiang seemed possible in the early summer, but came to nothing; Yang's star appeared to be on the wane,

but towards the end of the year he came once more to the forefront of Szechuan politics, when he was appointed to the Provincial Government by Nanking, at the same time enlarging the sphere of his military control at the expense of General Lo Tse-chow.

Yang Wen-k'ai. 1926.

Yang Yü-t'ing. 1925–26–27–28. It has transpired since his death in January 1929 that he played an important part in the assassination of Chang Tso-lin in the hope of usurping power himself. This was possibly the reason for the drastic treatment meted out to him by Chang Hsueh-liang.

Yeh Ch'u-ts'ang. Born in 1883 at Kiangsu; editor of various papers; 1926 acting chief secretary, Kuomintang Central Political Council; 1928–29 member of the Kiangsu Provincial Government and concurrently Commissioner of Reconstruction; Director of Publicity, Central Kuomintang Headquarters; April 1930 appointed chairman of the Kiangsu Provincial Government. Member of Kuomintang Central Executive Committee and Central Political Council.

Yeh K'ai-hsin. 1926-27.

Yeh T'ing. 1927.

Yen Hsi-shan. 1925-26-27-28-29. His attitude at the beginning of the year was one of marked but overt hostility to Chiang Kai-shek, and, although on the 22nd January he accepted the title of Vice-Commander-in-chief of the Army, Navy and Air Forces, a military conference was held at Tai Yuan early in Yen, however, hesitated to plunge into actual warfare until the attitude of Mukden was known, and he was faced with the dilemma of joining forces with the extreme left wing of the Kuomintang or of currying favour with Mukden. He made the fatal blunder of over-estimating the popular dislike of Chiang Kai-shek. When the neutrality of Mukden seemed assured, all semblance of Nanking control in Hopei and Shansi disappeared, Yen in March ordering the dissolution of all Tangpu organs, at the same time resigning all his posts under Nanking. He assumed the title of Commander-in-chief on the 1st April. The State Council thereupon issued a mandate denouncing him as "craftiness and falsehood personified," dismissed him from all his posts and ordered his arrest. The first clashes took place in May, and fighting continued with varying success throughout the summer, but the action of Chang Hsueh-liang in September in sending troops to occupy Tientsin caused Yen to remove his newly-formed Government from Peking to Tai Yuan. Fighting virtually ceased in October, and in November Yen withdrew from the political stage, fleeing secretly to Tientsin in December and leaving the country. Thus ended (perhaps only temporarily) the career of the Model Tuchun, who for so many years had kept his province prosperous and free from civil war, but who was at last induced by the force of circumstances and his own ambitions to attempt the disastrous experiment of enlarging the sphere under his control.

Yen Hui-ch'ing (W. W. Yen). 1925–26. Appointed adviser to the Ministry for Foreign Affairs in 1928.

Yu Hsueh-chung. Native of Shantung. Trained for a military career; at one time an adherent of Wu Pei-fu, he was later taken over by Fengtien; 1927 Commander-in-chief, Chingchow and Liaoyang defences; 1928 adviser, North-Eastern Defence Headquarters; 1930 commander of the North-Eastern Defence, Ist Army; October 1930 appointed garrison commander, Peking and Tientsin Garrison. Not a native of Manchuria, his loyalty to Chang Hsueh-liang is not altogether free from suspicion. Understood still to have affiliation with Sun Ch'uan-fang.

Yü Ya-ch'ing (Yü Hsia-ch'ing). 1925–26. Member of the Shanghai Municipal Council and instrumental in a final settlement of the 30th May, 1925, incident being reached.

Yuan Tsu-ming. 1926.

Yueh Wei-chun. 1925-26.

Yun Ta-ying (Yuin Dai-ying). 1926.